EIOPA-BoS-14/061
21 May 2014

# Discussion Paper

# Conflicts of Interest in direct and intermediated sales of insurance-based investment products (PRIIPs)

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# 1. Responding to the Discussion Paper

EIOPA welcomes comments on the Discussion Paper on the Conflicts of Interest in direct and intermediated sales of insurance-based investment products (PRIIPs).

The package includes:

- The Discussion Paper;
- Template for comments.

Please send your comments to EIOPA in the provided Template for Comments, by email to DP-14-IMD@eiopa.europa.eu, by 22 July 2014, 18:00 CET.

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

**Publication of responses**

All contributions received will be published following the close of the consultation, unless you request otherwise in the respective field in the template for comments. A standard confidentiality statement in an email message will not be treated as a request for non-disclosure. A confidential response may be requested from us in accordance with EIOPA's rules on public access to documents. We may consult you if we receive such a request. Any decision we make not to disclose the response is reviewable by EIOPA's Board of Appeal and the European Ombudsman.

**Data protection**

Information on data protection can be found at www.eiopa.europa.eu under the heading 'Legal notice'.

# 2. Executive Summary

The Discussion Paper is intended to help facilitate a public consultation. It includes all necessary information on the consultation process. The scope and objectives of the public consultation follow the mandate from the European Commission to EIOPA for technical advice concerning amendments related to conflicts of interest made by Article 91 of the Markets in Financial Instruments Directive (MiFID II)[1] to the Insurance Mediation Directive (IMD).[2]

[1] The text referred to here is the text of the political agreement reached between the European Parliament and the Council revised by legal revisers and adopted by the European Parliament at the plenary session on 15 April 2014 but not yet published in the Official Journal. See http://www.europarl.europa.eu/sides/getDoc.do?type=PV&reference=20140415&secondRef=ITEM-017-08&language=EN&ring=A7-2012-0306 for further details.
[2] EU Directive 2002/92: http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:32002L0092:EN:HTML

The aim of the Discussion Paper is twofold. First, to provide stakeholders with an early orientation on issues that will need to be addressed in the technical advice of EIOPA to the Commission. Second, to gather feedback from all stakeholders on these issues. A further consultation on the draft technical advice will follow following this first round of feedback.

The Discussion Paper focuses solely on conflicts of interest as introduced by the amendments to the IMD. The rules on conflicts of interest require insurance undertakings and insurance intermediaries to make organisational and administrative arrangements to prevent conflicts from harming customers. These rules relate solely to insurance distribution activities for insurance-based investment products. They cover insurance undertakings making direct sales, as well as insurance intermediaries. They do not cover sales of non-life insurance products, sales of pure protection life insurance products, or sales of life insurance products used for personal pensions.

The possibility of banning third party payments such as commissions is outside the scope of this Discussion Paper, as this is explicitly addressed in the amendments to the IMD as a matter for potential rules at the Member State level. However, other measures to manage and mitigate such arrangements so that they do not harm customers, as might be taken in the absence of a ban, are within the scope of this Discussion Paper.

The Discussion Paper sets out the amendments, and explains from a high level what conflicts of interest are and why they matter. Conflicts of interest are situations in which those undertaking insurance distribution activities have an interest of their own that is not aligned with the best interests of customers. Conflicts of interest can also materialise between the interests of different groups or types of customer. Furthermore, they are not limited to the pre-contractual phase of a contractual relationship, but may also relate to issues that arise following a contractual commitment. While conflicts of interest might exist, they become material where they lead to harm for customers. Preventing such harm is important in fostering strong consumer protection in relation to financial services in the European Union.

The detailed part of the Discussion Paper is split according to the two parts of the empowerment for the European Commission:

- criteria for identifying types of conflict of interest that might harm customers; and
- steps to be taken in identifying, preventing, managing and disclosing conflicts of interest.

The European Commission requests EIOPA to use in both cases the measures already developed at EU level under equivalent empowerments within MiFID as

its starting point, as set out in the MiFID Implementing Directive.[3] The European Commission requests that EIOPA works closely with ESMA to ensure as much cross-sectoral consistency as is possible. This includes taking into account potential proposals from ESMA for changes to the MiFID Implementing Directive pursuant to MiFID II, in so far as these are consistent with the amendments made to the IMD. Such proposals will be considered once they have become available.

Specific issues arising related to insurance distribution activities should also be taken into account. The Discussion Paper identifies two areas in particular: questions on proportionality and on the handling of third party payments ('inducements').

- Proportionality arises in particular in regards specifying the steps to be expected of very small intermediaries, which dominate insurance distribution in some markets, and where certain measures are not possible, such as physical separations between functions.
- Third party payments and benefits, including 'hard' and 'soft' commissions, are a common feature of insurance distribution activities in many markets. As already noted, a blanket ban on such payments or benefits is not within the scope of this Discussion Paper or the empowerments given to the European Commission. Other measures related to preventing harm for customers due to such payments are however within the scope of this Discussion Paper, and feedback is sought from stakeholders on them.

The Discussion Paper also seeks input from stakeholders on assessing impacts of possible changes in this area.

If you would like to comment, please send your comments to EIOPA in the provided Template for Comments, by email to DP-14-IMD@eiopa.europa.eu, by 22 July 2014, 18:00 CET.

[3] Commission Directive 2006/73/EC: http://eur-lex.europa.eu/LexUriServ/LexUriServ.do?uri=CELEX:32006L0073:EN:NOT, see Art 21 onwards

# 3. Background to Discussion Paper

This Discussion Paper reflects a Mandate for technical advice received formally from the European Commission on 21 May, attached as Annex 4.

The Mandate follows amendments to the IMD by MiFID II. These amendments are contained within Article 91 of MiFID II, which introduces into the IMD, for the sale of insurance-based investment products, certain elements of the conduct of business rules contained within MiFID. Insurance-based investment products are defined in the amendments, and cover life-insurance contracts which have a "maturity or surrender value [that] is wholly or partially exposed, directly or indirectly, to market fluctuations". Pure-protection, non-life insurance and personal or private pensions in the form of insurance contracts are not covered.

Recital 87 of the MiFID II text outlines the importance of consistent protection standards for retail clients, and of ensuring "a consistent regulatory approach concerning the distribution of different financial products which satisfy similar investor needs and therefore raise comparable investor protection challenges". Market structures and product characteristics make it more appropriate to include this "consistent regulatory approach" as part of the IMD. Recital 88 states that in order to achieve alignment, the IMD should be amended already in the areas covered by Article 91: "the rules pertaining to conflicts of interests, general principles and information to customers and to allow Member States to place restrictions on the remuneration of insurance intermediaries".

This Discussion Paper is concerned solely with the amendments related to **conflicts of interest** and in particular the preparation of technical advice to the European Commission related to **delegated acts** in this area ('level two' measures).

The aim of the Discussion Paper is to provide stakeholders with an early orientation on possible issues to be addressed in the technical advice of EIOPA to the Commission on these delegated acts, and to seek feedback from all stakeholders. The Paper identifies certain existing and potential conflicts of interest that have arisen or may arise in the direct or intermediated sale of insurance-based investment products, examines potential measures for addressing these conflicts, and sets out a high-level assessment of impacts for different stakeholders.

For the avoidance of doubt, the extent to which Member States should apply blanket bans on third party payments and benefits are not within the scope of this Discussion Paper. Such payments and benefits are not banned *per se* under the amendments, which instead explicitly permit Member States to impose rules to do so themselves. The Discussion Paper considers instead conditions under which such payments and benefits may be made in the absence of such bans, and steps to be taken to mitigate conflicts of interest that thereby might arise. Section 4 sets out more details on this.

*Previous work*

Previous work has been undertaken on conflicts of interest related to PRIIPs (packaged retail and insurance-based investment products) by the three predecessors to the European Supervisory Agencies, the Committee of European Insurance and Occupational Pension Supervisors (CEIOPS), the Committee of European Banking Supervisors (CEBS) and the Committee of European Securities Regulators (CESR), (collectively known as the three level three committees or 3L3).[4] This work formed a basis for proposals from the European Commission, and included a specific section on possible future 'level two' measures on conflicts of interest. The relevant section of the document is excerpted as Annex 3 below.

The measures proposed within the 3L3 Report[5] are in substance very close to those contained in the MiFID Implementing Directive. The MiFID measures apply to investment firms, including both large and very small firms, and not insurance undertakings or insurance intermediaries (natural or legal persons), though any such entities that undertake activities that fall within the scope of MiFID would be subject to MiFID, exceptions to MiFID notwithstanding.

The European Commission requests in its mandate to EIOPA for technical advice that EIOPA takes into account potential proposals from ESMA for changes to the MiFID Implementing Directive pursuant to MiFID II, in so far as these are consistent with the amendments made to the IMD. Such proposals will be considered once they have become available, and so are not addressed in this Discussion Paper.

# 4. Detail of the amendments

The text of Article 91 containing the amendments, and accompanying recitals, can be found in Annex 1.

The amendments made by Article 91 of MiFID II to the IMD are applied to distributors of insurance-based investment products, both insurance intermediaries and insurance undertakings. The inclusion of insurance undertakings is a significant change to the IMD under this amendment, a change that was also part of the IMD2 proposal of the Commission.[6]

The changes apply solely to the distribution of insurance-based investment products. A definition of these is inserted into the IMD under IMD Article 2(3). This definition would appear to be the same as that included also in the recently

[4] http://eiopa.europa.eu/fileadmin/tx_dam/files/publications/submissionstotheec/20101012-3L3-TF-Report-on-PRIPs.pdf, see p. 39-40.
[5] See also the CEIOPS advice to the Commission in relation to the revision of the IMD, though the policy context was materially different to the policy context in which this Discussion Paper has been prepared: http://eiopa.europa.eu/fileadmin/tx_dam/files/publications/submissionstotheec/20101111-CEIOPS-Advice-on-IMD-Revision.pdf, see p 66 -.
[6] See http://ec.europa.eu/internal_market/insurance/docs/consumers/mediation/20120703-directive_en.pdf.

agreed text for the introduction of a Key Information Document for PRIIPS.[7] Amongst other things, the non-life insurance products and pure-protection life insurance products are not within scope.

Note that the changes are cumulative with other measures in the IMD. Notably, IMD Articles 12 (1)(c) and 12(1)(d) require disclosures where a distributor has a holding of more than 10% of an insurance undertaking, or vice-versa. Article 12 also requires disclosure where the intermediary is under the contractual obligation to conduct insurance mediation business exclusively with one or more insurance undertakings. Disclosure pursuant to Article 12 is not to be confused with disclosures under the amendments. Articles 12 and 13 will both apply.

The key changes made by Article 91 are:

- A new **Article 13b**, requiring intermediaries or insurance undertakings to 'maintain effective organisational and administrative arrangements' for preventing conflicts of interest from adversely affecting the interests of their customers (as determined also be new Article 13c);
- A new **Article 13c**, requiring:
    - Appropriate steps to be taken to identify conflicts of interest between intermediaries or insurance undertakings and their customers. This includes those linked by control to the intermediary or the insurance undertaking;
    - Where organisational and administrative arrangements to manage conflicts may not be sufficient to prevent conflicts negatively impacting customers (as under Article 13b), a disclosure must be made.
- An empowerment for the Commission under **Article 13c (3)**, to adopt **delegated acts**:
    - To identify steps to be taken by insurance intermediaries or insurance undertakings to identify, prevent, manage and disclosure conflicts of interest related to insurance distribution activities;
    - To set criteria for the types of conflict of interest that could damage customer interests.
- A new **Article 13d** which establishes the principle of 'acting in the best interests of the customer' and an obligation that information for customers is 'fair, clear and not misleading' (whether marketing information or not);
- An allowance under **Article 13d (3)** that "Member States may prohibit the acceptance or receipt of fees, commissions or any monetary benefits

[7] The final text has not yet been published in the Official Journal. See http://www.europarl.europa.eu/oeil/popups/ficheprocedure.do?lang=en&reference=2012/0169(COD).

paid or provided to insurance intermediaries or insurance undertakings, by any third party or a person acting on behalf of a third party in relation to the distribution of insurance-based investment products to customers".

Member States shall have 24 months from the date of entry into force of the MIFID II Directive to transpose into national law changes pursuant to these amendments.

***Discussion of amendments***

The amendments require insurance undertakings and insurance intermediaries to make organisational and administrative arrangements to prevent conflicts from harming customers.

The organisational and administrative arrangements should in the first instance aim to **avoid conflicts** happening, for instance by separating roles or functions.

While not all conflicts might be avoided, those conflicts that are not avoided in the first place must instead be **managed** or **mitigated**, so as to prevent them from harming the interests of the customer. For instance, this might be by placing limits on commission payments where the payments are not clearly for the benefit of the customer, or avoiding volume-based remuneration arrangements, e.g. contingent commissions.

Disclosure of conflicts of interest is a final step where avoidance or management has not succeeded. Disclosure is clearly separate from the steps necessary to avoid or manage conflicts.

The application of these amendments to commission payments or arrangements is of particular significance, given their importance in a number of markets for insurance distribution activities related to insurance-based investment products.

The amendments allow for Member States to impose a specific ban on third party payments (commissions or inducements). For this reason, such *per se* bans are not addressed by this Discussion Paper. However, this Discussion Paper is addressing, *inter alia,* the question as to how conflicts of interest arising out of remuneration arrangements might be avoided, mitigated, managed or disclosed, where Member States have not decided to impose a ban at national level. While the drafting of Article 13d (3) makes it clear that payment of commissions and other third party payments cannot be taken *per se* to always harm customers, such payments nonetheless can create conflicts of interest which in the absence of management may lead to harm for customers.

The amendments apply to the full range of entities engaged in insurance distribution activities. These include, among others, both sole-trading[8] insurance

[8] "Sole Trader", in this context, is a natural person, in other words a person who runs a business by himself/herself.

intermediaries and large insurance undertakings, which must take organisational and administrative steps to prevent conflicts impacting the interests of customers, and take steps to identify, prevent, manage and disclose the conflicts.

However, the amendments do not require the detailed nature of these steps – as may be specified through implementing measures – to be the same irrespective of the size and nature of the business of the entity.

# 5. What are conflicts of interest?

In general, conflicts of interest occur when an entity has an interest of its own that conflicts with the interest or interests of other customers or entities for whom the entity is also acting in some capacity. Conflicts of interest can exist without harm for the customer, for instance where a conflict is identified and managed or mitigated by the entity suffering the conflict so as to ensure there is no harm for the customer.[9]

For example, an intermediary has an interest in its own financial success. This success may depend on payments from insurance undertakings, for instance related to sales volumes. This might lead the intermediary to propose products that do not best match the demands and needs of the customer, but which instead pay the intermediary higher commissions, whether directly or indirectly. In this case a conflict of interests exists, and where products are sold that are not matching the demands and needs of the customer, harm for the customer is occurring, indicating a failure to manage the conflict of interests.

- Monetary relations are a key driver of conflicts. These relations may be between separate entities (for instance, an insurance undertaking and insurance intermediary, whether independent or tied, and in the form of payments of commissions (whether one-off or ongoing in form) to these latter by the former for sales) or within a single insurance undertaking or between connected companies (for instance, direct sales forces being rewarded by bonuses for sales of particular product lines).
- For some conflicts, indirect monetary relations could be the driver. These include so-called soft-commissions (e.g., provision of office equipment, training, defraying of other costs an entity would otherwise incur).
- There are drivers for conflicts that are less easily summarised as monetary in nature. For instance, conflicts arising from personal relationships between individuals or their families working in different organisations or parts of organisations.

[9] Throughout this Discussion Paper references to customer may be interpreted, where this might be relevant, to cover beneficiaries, insured persons and policyholders. In general, for insurance-based investment products these will often be the same person, but this may not always be the case.

Some conflicts of interest relate to conflicts between the interests of different groups or types of customers, for instance between existing customers and new customers, or customers for different classes of product (who may drive different levels of remuneration for the seller).

Conflicts of interest are also not limited to the pre-contractual phase of a contractual relationship, but may also relate to issues that arise following a contractual commitment, for instance in relation to on-going disclosures. In this regard it should be recalled that insurance mediation (which forms the basis for 'insurance distribution activities') is defined in Article 2 (3) of the IMD as "the activities of introducing, proposing or carrying out other work preparatory to the conclusion of contracts of insurance, or of concluding such contracts, or of assisting in the administration and performance of such contracts, in particular in the event of a claim".

# 6. Why do conflicts of interest matter?

The impact assessment work of the Commission in support of the revision of the IMD outlined the Commission's conclusion – consistent with academic work on financial education and financial capabilities of consumers - that most customers of financial services, including those buying insurance-based investment products, suffer from deep asymmetries of information, such that they often are dependent on advice from those selling to them and are not well able to assess any limitations to the advice provided.[10] The Commission viewed this as particularly relevant for packaged products, including insurance-based investment products. The Commission concluded in its impact assessment on the revision of the IMD that "a lack of action at EU level [in relation to the IMD] will likely result in an increase in the number of cases of mis-selling of insurance products and cases where consumers are led to take undue risks".[11]

Given the importance of advice in such sales, the Commission concluded that it would be of key importance, amongst other steps, to ensure that professional and quality advice is given to consumers, and the Commission's assessment was that strong and effective rules on conflicts of interest were an essential element in achieving this.[12] The Commission's focus on conflicts of interest reflected the assessment that unmanaged or unmitigated conflicts of interest have the potential to undermine the quality and professionalism of advice and its alignment with the best interests of the customer. The Commission, in addition,

[10] See this study for much further detail on some of the issues faced by consumers in relation to financial services products, including insurance-based investments: http://ec.europa.eu/consumers/archive/strategy/docs/final_report_en.pdf.
[11] See http://ec.europa.eu/internal_market/insurance/docs/consumers/mediation/20120703-impact-assessment_en.pdf, p. 21, see in general pp. 19-21. See also http://ec.europa.eu/internal_market/consultations/docs/2010/prips/costs_benefits_study_en.pdf.
[12] This conclusion was already highlighted in http://ec.europa.eu/internal_market/consultations/docs/2010/prips/costs_benefits_study_en.pdf, and underlined in http://ec.europa.eu/internal_market/insurance/docs/consumers/mediation/20120703-impact-assessment_en.pdf.

concluded that a lack of a level playing field between sectors – that is, consistent steps to address conflicts of interest throughout the financial services – could lead to distortions and regulatory arbitrage.

Another, more general, perspective may be of interest. Ongoing market monitoring for the purposes of a Commission consumer market 'scoreboard' has shown that financial services are routinely at the bottom in terms of performance (as measured across a number of dimensions).[13] Banking services score lower than insurance services in this assessment, but both are low.

This low level reflects the scale of the work that needs to be done to improve the performance of financial services from the perspective of the consumer.

# 7. Current situation

In examining different possible options, it is important to develop a clear picture of the existing situation across the EU. EIOPA has already gathered, on an informal basis, input from national supervisory authorities on this existing situation. Given that the IMD is minimum harmonising, Member States have the capacity to apply additional rules, creating the opportunity for significant variations across the EU.[14] In addition, regulatory standards applicable to conflicts of interest in insurance distribution activities by insurance undertakings have not so far been subject to harmonisation at the EU level.

According to input gathered, half of respondents are aware of measures on mitigating conflicts of interest introduced through industry-led initiatives. National supervisory authorities have different views as to these initiatives. Some have taken a view that the industry-led initiates have not been sufficient to fully address potential sources of harm. In some Member States, the industry-led initiatives have been picked up or supplemented by national supervisory authorities. For example, industry steps might have sought to address conflicts of interest in traditional remuneration schemes, to be followed by a ban on specific inducements, so that voluntary rules have been reinforced by mandatory rules. It is noteworthy that, even though industry-led initiatives are in place, four in five Member States have additional rules on conflicts of interest.

Some Member States have extended rules of a similar kind to MiFID to apply to insurance intermediaries and/or undertakings. Almost one in six of the respondents who replied noted that they have extended the most important

[13] See "investment products, private pensions and securities" category, see http://ec.europa.eu/consumers/consumer_research/editions/docs/8th_edition_scoreboard_en.pdf and http://ec.europa.eu/consumers/consumer_research/editions/docs/monitoring_consumer_markets_eu_2012_en.pdf. Insurance more generally is listed separately (and does slightly better than banking), but arguably most PRIIPs would fall under the 'investment products, private pensions and securities' category, rather than the 'private life insurance' category.

[14] IMD Article 12 (5) specifically states "Member States may maintain or adopt stricter provisions regarding the information requirements referred to in paragraph 1, provided that such provisions comply with Community law."

MiFID rules to insurance intermediaries and insurance undertakings, including on conflicts of interest. One respondent outlined the steps, for instance, that they have put in place on establishing independence of functions so as to mitigate conflicts of interest. Another Member State along similar lines required insurance undertakings to ensure that there are effective 'Chinese walls' in place.

Other binding national initiatives have been developed however. A significant number of Member States have extended the scope of the IMD and/ or have applied measures on conduct or conflicts to insurance undertakings and insurance intermediaries, but which are different from those in MiFID. Those regulatory binding measures are varied. For example, a few Member States have rules in place to scrutinize registration of insurance intermediaries and insurance undertakings to avoid conflicts of interest. Some have gone beyond MiFID by banning all inducements (whereas MiFID does not apply an outright ban).

One in five Member States have chosen not to enact additional national binding legislation, over and against what is required under the IMD.

The setting of national binding legislation on conflicts of interest where national supervisory authorities have so chosen is only part of the current situation. Among other instruments, national supervisory authorities also have a strong role in shaping the rules on conflicts of interest for insurance undertakings and insurance intermediaries via 'soft' law and guidance. Almost every national supervisory authority is addressing the topic in one way or another.

In this regard, authorities have taken a wide variety of tangible supervisory measures. Half of them used guidelines or guidance via letters with recommendations to address conflicts of interest in their jurisdiction. One in five authorities put a strong focus on the compliance with rules on conflicts of interest. They used mostly inspections, mystery shopping and thematic reviews to assess the level of compliance. A majority of the authorities who focussed on conflicts of interest, responded to infringements by issuing fines and sanctions.

At the level of supervised undertakings themselves, some respondents noted that some of them will be authorised both as insurance intermediaries and as MiFID firms, though quantitative data was not provided at this stage. These undertakings will already, for the part of their business subject to MiFID rules, be subject to conflicts of interest measures under MiFID. Those entities may well have extended, where this is consistent with national law, their own organisational and administrative arrangements for addressing conflicts of interest to cover all areas of their business, so as to maintain consistent compliance standards. Others will not have done this, or are only authorised for insurance distribution activities. Note that Member States have different approaches to the organisation of the supervision of entities that have been authorised both under MiFID and for insurance distribution activities.

The current situation is therefore varied across different jurisdictions and between the handling of different entities involved in insurance distribution activities.

# 8. The call for technical advice from the European Commission

The Mandate from the European Commission is attached below as Annex 4.

The Mandate sets out key principles that EIOPA is invited to take into account under section 1.2. These include working with ESMA "to achieve as much consistency as possible in the conduct of business standards for insurance-based investment products"; taking into account internal market dimensions, a high level of consumer protection, and the principle of proportionality.

The Mandate is structured in accordance with the relevant empowerments.

It covers first the steps to identify, prevent, manage and disclose conflicts.

Here EIOPA is requested to start its work on the basis of the existing conflicts of interest measures contained in the MiFID Implementing Directive. The Mandate highlights potential conflicts of interest related to remuneration and third party payments and benefits as key areas to be covered, inviting EIOPA to consider identifying "remuneration or commission arrangements that lead to harm for the customers' interests and ways of avoiding these, or where avoiding these is not possible, examine monitoring, or placing conditions or limitations on conduct and other arrangements that aim to limit harm to customers' interests". It also explicitly requests technical advice on the content and quality of disclosures (including when online) in view of enabling customers to make informed investment choices, and for measures on the periodic review of conflicts of interest policies.

The Mandate specifically invites EIOPA to engage in "regular consultation with ESMA as regards ESMA's work on its technical advice on Article 23 (4) (a) and (b) of MiFID II. In this respect, the EIOPA advice should be in line with the MiFID II Level 2 provisions as much as possible, in so far as it is consistent with IMD 1.5."

It then covers the criteria for identifying types of conflict of interest that might damage the interests of customers. In regard to this, the Mandate highlights the variety of channels and products to be covered. It also mentions conflicts of interest issues that might arise during the lifetime of the product (not only at the point of sale). As with the first empowerment, the Mandate invites EIOPA to work on the basis of the existing criteria on types of conflicts of interest contained in the MiFID Implementing Directive.

The deadline for EIOPA to provide its advice to the European Commission is set to seven months following the entry into force of MiFID II.

# 9. Detailed examination of empowerment: Types of conflict of interest

**Empowerment**

… to establish appropriate criteria for determining the types of conflict of interest whose existence may damage the interests of the customers or potential customers of the insurance intermediary or insurance undertaking.

**Mandate**

*"With a view to establishing appropriate criteria for determining the types of conflict of interest whose existence may damage the interests of the customers or potential customers of insurance-based investment products, EIOPA is invited to verify to what extent the criteria in Directive 2006/73/EC need to be adapted and/or supplemented for insurance-based investment products.*

*Different products as well as different distribution channels might present different conflict of interest risks. EIOPA should also consider the timeframe of insurance-based investment products - notably what the conflict of interest issues are at the point of sale as well as during the products' lifetime.*

*EIOPA should consider that conflicts of interest are often related to the remuneration/inducements received by the insurance intermediary or insurance undertaking and therefore an essential element in designing the conflict of interest rules. As the Directive establishes a similar framework for ESMA as regards conflicts of interest, EIOPA is invited to closely liaise with and consult ESMA when providing the technical advice to the Commission."*

**MiFID Implementing Directive**

*Article 21*
*Conflicts of interest potentially detrimental to a client*

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

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

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

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

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

(e) the firm or that person receives or will receive from a person other than the client an inducement in relation to a service provided to the client, in the form of monies, goods or services, other than the standard commission or fee for that service.

***Discussion***

The empowerment is to clarify criteria for identifying different types of conflicts of interest. A condition is applied as to whether these may damage customers' interests. It is also a prospective condition: the damage may not have happened in the past, but the test relates to damage that could happen. The empowerment does not refer to the likelihood or scale of possible damage.

The measures in the MiFID Implementing Directive are drafted in a general and high level manner to cover the different types of conflicts that might lead to harm for customers, such that they are broadly applicable also to insurance distribution activities. These follow the broad logic outlined above in in section 5 above. For example:

- Certain terms would need to be adapted for the purposes of application to insurance distribution activity: 'investment or ancillary service' would need to be replaced by the concept of 'insurance distribution activity'; 'investment firms' by 'insurance undertakings and/or insurance intermediaries'; and 'client' by 'customer';
- The concept of a 'relevant person' may also need to be defined, as this is a defined term in the MiFID Implementing Directive.

The 3L3 report and the CEIOPS advice on IMD2, refer to similar broad types of possible conflicts, but included detail on the conflicts of interest that is more tailored to insurance distribution activities. Also, initial fact-finding amongst national supervisory authorities by EIOPA confirms this.

Those identified in the 3L3 report repeated in substance the types of conflicts outlined in MiFID, but **also** included the following more specific insurance instances:

- Registration as an insurance intermediary in more than one category (with different levels of formal independence), or simultaneously as a reinsurance and insurance intermediary, which may give rise to arbitrary placement of insurance contracts. For example, broker/agent where an intermediary is both a broker (and thus representing interests of prospective insurance policy holder) and an agent (also taking into consideration the interests of insurers). *Note however that under the amendments to the IMD, agents are required to act in the best interests of the customer, and cannot be seen as solely representing the interests of insurers;*

- The distributor's interest in the insurance contract (e.g. in relation to which he is a beneficiary; occurring, for instance, in situations where a bank registered as an insurance intermediary is a beneficiary of a life insurance associated to a mortgage) potentially conflicting with the insured person's contractual interest.

The CEIOPS advice to the Commission on the IMD revision included other examples that appear relevant:

- Intermediaries who fulfil functions for third parties (e.g. as members of the governing bodies or fixed staff of an insurance or reinsurance undertaking; as appointed actuaries or auditors of insurance or reinsurance undertakings) acting more in the interests of these third parties than the customer;
- Personal ties, such as where individuals linked by family have different positions in insurance intermediation or are employed by an insurance undertaking, leading the seller to act in the interest of the linked individual than the customer;
- Selling insurance products in association with the supply of other products or services, where commission payments on linked business have led to the seller acting in their own interest rather than that of the customer;
- Contingent commissions, profit shares, or volume over-riders leading an intermediary to act in their own interest rather than that of the customer;
- Soft commissions (corporate hospitality and gifts, soft loans, training support, administrative support) leading an intermediary to act in their own interest rather than that of the customer;
- Remuneration linked to sales-volumes leading to the seller acting in their own interest rather than that of customer;
- Successful sales of one line of product acting as a 'sweetener' for access to other, higher-commission products, leading an intermediary to act in their own interest rather than that of the customer;
- Intermediaries being actively involved in the design of an insurance product and being at the same time the (main) distributor of that product;
- Minimum levels of sales being required from an intermediary in order to be accepted as an intermediary by the insurer.

Fact-finding by EIOPA amongst national supervisory authorities has highlighted many of the same types of conflict. In general, responses have underlined the central importance of conflicts linked to remuneration (including commissions). A number of the responses highlighted conflicts of interest between classes or types of customers – for instance, between existing customers and new customers. Conflicts of interest arising because of interests across a group

structure, including where parts of the group are not insurance undertakings or intermediaries, were also highlighted by some of the respondents. It was noted that since investment-based insurance products might be a significant source of funding at group level, these could constitute material conflicts in practice. Group issues were highlighted across all cases where types of links existed between the seller and other entities, where these links might impact the behaviour of the seller.

Other types of conflict mentioned included those linked to tying and bundling practices and similar relationships, where, for instance, an insurance contract (including an investment-based insurance product) is sold as a condition for another product, or vice-versa. Other specific situations were mentioned, for instance relating to certain 'subscriber broker' structures in a particular market. Cases were also mentioned where sellers might be both a party to an insurance contract and an intermediary in the sale of the contract. That could be, for example, the case for certain banks.

Analysis of the underlying types of these different conflicts of interest would suggest they might be seen always as specific instances or examples of conflicts of interest that still might broadly fall under the broad types of conflicts of interest set out the MiFID Implementing Directive.

However, the general nature of the drafting of the criteria in MiFID Article 21 means it is not always clear how it would apply to specific insurance distribution activities and the structures and inter-relations of insurance undertakings and insurance intermediaries, as identified in the above lists.

For this reason, the high level types of conflicts outlined in MiFID could be further developed for the purposes of addressing the specific types of conflicts arising for insurance undertakings and insurance intermediaries, by including the lists – further elaborated in the light of responses to the Discussion Paper – within the body of implementing measures under the IMD, for instance as non-exhaustive indicative examples or instances of types of conflicts of interest.

**Questions on types of conflict of interest related to insurance distribution activities**

1. What types of conflicts of interest have you experienced in practice or are aware of?

   For each type of conflict, please identify in your view the cause of the conflict, who (in general terms) it applied to, and, where possible, provide an assessment of its potential impact for customers.

2. What types of conflicts of interest do you believe are most important and why?

3. Are you aware of potential types of conflicts of interest other than those outlined in the discussion above?

4. More specifically, what conflicts of interest are you aware of that are related to insurance distribution activities undertaken following the conclusion of a contract (that is to say, during the life of the contract or after it ends)?

   Please identify the type and source of the conflict and include any data available on the incidence and impact of the conflict.

5. Do you agree that specific types of conflicts of interest for insurance distribution should be added to the basic structure contained within Article 21, as outlined in the discussion above?

   If so, please clarify which types, and how they might be different from the types of conflict already covered by the criteria in Article 21.

6. Are there any other adjustments that might need to be made to the criteria in Article 21 to clarify their application?

   Where you believe an adjustment is necessary to clarify the application of the criteria, please explain the adjustment you propose.

7. Do you have any other comments on the assessment of possible criteria for identifying types of conflicts of interest set out above?

# 10. Detailed examination of empowerment: steps to be taken in identifying, preventing, managing and disclosing conflicts of interest

**Empowerment**

… to define the steps that insurance intermediaries or insurance undertakings might reasonably be expected to take to identify, prevent, manage and disclose conflicts of interest when carrying out insurance distribution activities.

**Mandate**

*"Certain investment products, such as insurance-based investment products, can be sold or distributed in different ways by insurance intermediaries or insurance undertakings. There are certain existing or potential conflicts of interests arising in the distribution of these products. These can be similar to the conflicts of interests found in the field of investments, but might have additional or different characteristics.*

*Therefore, EIOPA is invited to base its technical advice primarily on existing conflicts of interest rules, as laid down in Commission Directive 2006/73/EC, while at the same time ensuring regular consultation with ESMA as regards ESMA's work on its technical advice on Article 23 (4) (a) and (b) of MiFID II. In this respect, the EIOPA advice should be in line with the MiFID II Level 2 provisions as much as possible, in so far as it is consistent with IMD 1.5.*

*In particular, EIOPA is invited to consider the existing conflicts of interest framework under Commission Directive 2006/73/EC and to develop a similar framework for insurance intermediaries and insurance undertakings distributing insurance-based investment products. EIOPA should consider identifying remuneration or commission arrangements that lead to harm for the customers' interests and ways of avoiding these, or where avoiding these is not possible, examine monitoring, or placing conditions or limitations on conduct and other arrangements that aim to limit harm to customers' interests.*

*In this context, EIOPA should also consider the framework for disclosure, including online disclosure, while identifying that disclosure is not a measure in itself to manage conflicts of interest. This should include how to devise content and how to ensure the quality of the information provided to customers in order to enable them to make an informed investment decision as regards insurance-based investment products.*

*EIOPA should also consider a requirement for periodical review of conflicts of interest policies or clarifications with respect to disclosure.*

*EIOPA is invited to consider in its technical advice the design of conflicts of interest frameworks to reflect the variety of the distribution channels that exist for the sale of insurance-based investment products. The size of firms carrying out the activity of insurance mediation should not alleviate responsibility on them from the obligation to devise a conflicts of interest policy."*

**MiFID Implementing Directive**

*Article 22*
*Conflicts of interest policy*

1. Member States shall require investment firms to establish, implement and maintain an effective conflicts of interest policy set out in writing and appropriate to the size and organisation of the firm and the nature, scale and complexity of its business. Where the firm is a member of a group, the policy must also take into account any circumstances, of which the firm is or should be aware, which may give rise to a conflict of interest arising as a result of the structure and business activities of other members of the group.

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

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

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

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

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

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

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

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

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

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

If the adoption or the practice of one or more of those measures and procedures does not ensure the requisite degree of independence, Member States shall require investment firms to adopt such alternative or additional measures and procedures as are necessary and appropriate for those purposes.

4. Member States shall ensure that disclosure to clients, pursuant to Article 18(2) of Directive 2004/39/EC, is made in a durable medium and includes sufficient detail, taking into account the nature of the client, to enable that client to take an informed decision with respect to the investment or ancillary service in the context of which the conflict of interest arises.

*Article 23*
*Record of services or activities giving rise to detrimental conflict of interest*

Member States shall require investment firms to keep and regularly to update a record of the kinds of investment or ancillary service or investment activity carried out by or on behalf of the firm in which a conflict of interest entailing a material risk of damage to the interests of one or more clients has arisen or, in the case of an ongoing service or activity, may arise.

*Article 24*
*Investment research*

1. For the purposes of Article 25, 'investment research' means research or other information recommending or suggesting an investment strategy, explicitly or implicitly, concerning one or several financial instruments or the issuers of financial

instruments, including any opinion as to the present or future value or price of such instruments, intended for distribution channels or for the public, and in relation to which the following conditions are met:

(a) it is labelled or described as investment research or in similar terms, or is otherwise presented as an objective or independent explanation of the matters contained in the recommendation;

(b) if the recommendation in question were made by an investment firm to a client, it would not constitute the provision of investment advice for the purposes of Directive 2004/39/EC.

2. A recommendation of the type covered by Article 1(3) of Directive 2003/125/EC but relating to financial instruments as defined in Directive 2004/39/EC that does not meet the conditions set out in paragraph 1 shall be treated as a marketing communication for the purposes of Directive 2004/39/EC and Member States shall require any investment firm that produces or disseminates the recommendation to ensure that it is clearly identified as such.

Additionally, Member States shall require those firms to ensure that any such recommendation contains a clear and prominent statement that (or, in the case of an oral recommendation, to the effect that) it has not been prepared in accordance with legal requirements designed to promote the independence of investment research, and that it is not subject to any prohibition on dealing ahead of the dissemination of investment research.

*Article 25*
*Additional organisational requirements where a firm produces and disseminates investment research*

1. Member States shall require investment firms which produce, or arrange for the production of, investment research that is intended or likely to be subsequently disseminated to clients of the firm or to the public, under their own responsibility or that of a member of their group, to ensure the implementation of all the measures set out in Article 22(3) in relation to the financial analysts involved in the production of the investment research and other relevant persons whose responsibilities or business interests may conflict with the interests of the persons to whom the investment research is disseminated.

2. Member States shall require investment firms covered by paragraph 1 to have in place arrangements designed to ensure that the following conditions are satisfied:

(a) financial analysts and other relevant persons must not undertake personal transactions or trade, other than as market makers acting in good faith and in the ordinary course of market making or in the execution of an unsolicited client order, on behalf of any other person, including the investment firm, in financial instruments to which investment research relates, or in any related financial instruments, with knowledge of the likely timing or content of that investment research which is not publicly available or available to clients and cannot readily be inferred from information that is so available, until the recipients of the investment research have had a reasonable opportunity to act on it;

(b) in circumstances not covered by point (a), financial analysts and any other relevant persons involved in the production of investment research must not undertake personal transactions in financial instruments to which the

investment research relates, or in any related financial instruments, contrary to current recommendations, except in exceptional circumstances and with the prior approval of a member of the firm's legal or compliance function;

(c) the investment firms themselves, financial analysts, and other relevant persons involved in the production of the investment research must not accept inducements from those with a material interest in the subject-matter of the investment research;

(d) the investment firms themselves, financial analysts, and other relevant persons involved in the production of the investment research must not promise issuers favourable research coverage;

(e) issuers, relevant persons other than financial analysts, and any other persons must not before the dissemination of investment research be permitted to review a draft of the investment research for the purpose of verifying the accuracy of factual statements made in that research, or for any other purpose other than verifiying compliance with the firm's legal obligations, if the draft includes a recommendation or a target price.

For the purposes of this paragraph, 'related financial instrument' means a financial instrument the price of which is closely affected by price movements in another financial instrument which is the subject of investment research, and includes a derivative on that other financial instrument.

3. Member States shall exempt investment firms which disseminate investment research produced by another person to the public or to clients from complying with paragraph 1 if the following criteria are met:

(a) the person that produces the investment research is not a member of the group to which the investment firm belongs;

(b) the investment firm does not substantially alter the recommendations within the investment research;

(c) the investment firm does not present the investment research as having been produced by it;

(d) the investment firm verifies that the producer of the research is subject to requirements equivalent to the requirements under this Directive in relation to the production of that research, or has established a policy setting such requirements.

*Article 26*
*Inducements*

Member States shall ensure that investment firms are not regarded as acting honestly, fairly and professionally in accordance with the best interests of a client if, in relation to the provision of an investment or ancillary service to the client, they pay or are paid any fee or commission, or provide or are provided with any non-monetary benefit, other than the following:

(a) a fee, commission or non-monetary benefit paid or provided to or by the client or a person on behalf of the client;

(b) a fee, commission or non-monetary benefit paid or provided to or by a third party or a person acting on behalf of a third party, where the following conditions are

satisfied:

(i) the existence, nature and amount of the fee, commission or benefit, or, where the amount cannot be ascertained, the method of calculating that amount, must be clearly disclosed to the client, in a manner that is comprehensive, accurate and understandable, prior to the provision of the relevant investment or ancillary service;

(ii) the payment of the fee or commission, or the provision of the non-monetary benefit must be designed to enhance the quality of the relevant service to the client and not impair compliance with the firm's duty to act in the best interests of the client;

(c) proper fees which enable or are necessary for the provision of investment services, such as custody costs, settlement and exchange fees, regulatory levies or legal fees, and which, by their nature, cannot give rise to conflicts with the firm's duties to act honestly, fairly and professionally in accordance with the best interests of its clients.

Member States shall permit an investment firm, for the purposes of point (b)(i), to disclose the essential terms of the arrangements relating to the fee, commission or non-monetary benefit in summary form, provided that it undertakes to disclose further details at the request of the client and provided that it honours that undertaking.

***Discussion***

The empowerment seeks a definition of the steps to take to identify, prevent, manage and disclose conflicts of interest when carrying out insurance distribution activities. There is a condition applied that these steps are what might be 'reasonably' expected of the distributor. This would appear to be an implied proportionality test.

The empowerment clearly separates the identification, prevention, management, and disclosure of conflicts.

Article 22 of the MiFID Implementing Directive requires a policy to be adopted by each firm. This policy must cover the identification and management of conflicts of interest: the firm is required to put in place the relevant procedures and measures. The policy must reflect the principle of proportionality (a number of criteria are to be considered in this context: the size and organisation of the firm and the nature, scale and complexity of its business). The identification of conflicts must also be guided by the material risk of harm.

Article 22 (3) establishes a key concept for the management of conflicts of interest, being the independence of functions. This is however itself required to be proportional to the size and activities of the firm and the materiality of the risk to customers. Article 22 (3) sets out certain indicative conditions for the application of the principle of independence to firms' activities or organisation.

As with the text on types of conflicts of interest, this text is again drafted in a relatively high level and general fashion, such that it might readily be adapted

for insurance undertakings and insurance intermediaries engaged in insurance distribution activities, following similar terminological refinements as for Article 21.

Articles 22 and 23 (which treats record keeping) are also broadly consistent with the indicative proposals within the 3L3 Report on PRIPs.

Articles 24 and 25 relate to investment research. The purpose of these articles is to address the specific conflicts that can arise where a firm is producing assessments of investment opportunities, other than personal recommendations that take into the account the specific circumstances and needs of an individual client. Such investment research may be distinguished from marketing information, and might be perceived by clients as independent and objective, yet without careful controls could in practice be exposed to and suffer from materially significant conflicts of interest. These issues can be expected to be important in relation to some insurance distribution activities where the insurance undertaking or insurance intermediary disseminates investment information that of a putatively neutral form; many insurance undertakings and insurance intermediaries will not be engaged in this.

Adapting Articles 24 and 25 for insurance distribution activities may require more changes, given these Articles include a number of cross references that are specific to MiFID that would need adjusting for the purposes of achieving a similar effect in the context of insurance distribution activities.

To begin with, two areas emerge where particular questions arise:

## 1. Proportionality

The drafting of Article 22 includes a principle of proportionality.

The measures in Article 22 (3) relating to the principle of independence are of particular interest in respect of sole traders and similar small intermediaries. These will often not have the organisational structure to be able to manage conflicts of interest through separations of functions (this may not be even possible in the case of intermediaries who are natural persons).

It may provide greater legal certainty and stronger harmonisation across the EU to specify the steps to be expected of such sole traders / small intermediaries.

## 2. Inducements

These are identified in Article 21 (e) as a criteria for identifying types of conflicts of interest.

The Article in the MiFID Implementing Directive related to the management of conflicts arising in relation to inducements is Article 26. This sets limitations on third party payments (inducements) in relation to investment services. Inducements are permitted, but only where certain conditions are met (notably a quality criterion that tests that the payment is to the benefit (in the interest) of the customer, and a disclosure requirement).

Inducements are not mentioned in Article 22 in MiFID, given the separation of inducements into a separate section, however, the conditions applied in Article 26 may be taken to be part of the steps necessary to manage the conflicts of interest created by inducement payments, as referred to in Article 21 (e).

**Questions on steps to identify, prevent, manage and disclose conflicts of interest related to insurance distribution activities**

8. Do you agree that additional measures might be necessary for clarifying how sole traders and similar entities might manage conflicts of interest, where independence of functions is not feasible?

   If so, please provide detail on the possible measures, explain why you believe these measures are appropriate, and set out how you believe these measures will effectively manage the conflicts of interest that might arise for sole traders and other similar entities.

9. Do you agree that it is necessary to include a further clarification of how to manage conflicts of interest arising out of third party payments or benefits, commission payments or remuneration?

   If so, please provide detail on the possible measures and the circumstances in which they might apply, explain why you believe these measures are appropriate, and set out how you believe these measures will effectively manage the conflicts of interest that might arise due to inducements or commission arrangements.

10. Do you have any other comments on the above assessment of the steps to take in relation to each of the following steps:

    - identifying conflicts of interest;
    - preventing conflicts of interest;
    - managing conflicts of interest; and
    - disclosing conflicts of interest?

11. Thinking specifically about disclosure, what steps do you think could maximise its effectiveness in ensuring customers understand and are able to use the information provided in their decision-making process?

12. Are there any additional adjustments to the existing MiFID measures in Articles 22 and 23 that might be necessary to clarify their application to

insurance distribution activities?

If so, please clarify which adjustments you believe necessary, set out why you believe this, and provide evidence to support your view.

13. Do you agree that the existing MiFID measures in Articles 24-25 related to investment research should be applied to insurance distribution activities, following a redrafting to take into account the legal framework applying to insurance undertakings and insurance intermediaries?

Please provide details of the aspects of insurance distribution activities to which you believe these measures might apply.

# 11. Identifying potential impacts of possible changes

***Indicative problem definition***

The underlying problem driver identified in the Commission work on PRIIPs, including for the IMD revision, is a combination of systematic asymmetries of information between customers and those selling PRIIPs to them, and principal-agent misalignments.

The level one measures on conflicts of interest are designed to ensure those selling insurance-based investment products avoid or mitigate principal-agent misalignments so that customer's interests are not harmed.

A secondary issue also highlighted by the Commission relates to cross-sectoral inconsistencies and the possible impact of regulatory arbitrage where regulatory measures are substantively different between different types of business, in particular where there is substitutability between those types of business. The Commission identified the market for insurance-based investment products and PRIIPs more broadly as a market where regulatory arbitrage had the potential to be a problem.

***Possible scope of level two options to be impacted assessed***

The empowerments that this discussion paper addresses relate to:

- Options for harmonising criteria for the identification of types of conflicts of interest;
- Options for harmonising steps to be taken to identify, prevent, manage and disclose conflicts of interest.

The Commission mandate makes clear that the starting point for this work shall be the MiFID Implementing Directive measures on conflicts of interest, and that options considered should be, as far as possible, consistent with this starting point.

The key issues therefore that need to be considered relate to different options or extents of harmonisation, based on the MiFID Implementing Directive measures, assessed against the asymmetries of information, level playing field, and principal-agent issues identified in the problem definition. The search is for measures to achieve effective management of conflicts of interests in the area of insurance distribution activities. The measures should minimise the possibility of regulatory arbitrage, whilst being appropriate and relevant to insurance distribution activities and the types of conflicts of interest that arise in relation to these activities.

Initial work suggests that different options on the harmonisation of the application of the proportionality principle may be particularly important, in view of the large number of small intermediaries (including intermediaries who are natural persons) involved in insurance distribution activities in a number of Member States. A second broad issue may be around possible measures to address conflicts arising through inducements or similar arrangements.

***Who is likely to be impacted?***

The universe of insurance distributors is particularly diverse, from small sole traders and brokers, through different types of agents, up to the employees of large insurance undertakings and bancassurers.[15]

All of these can be expected to be impacted by the changes made to the IMD, though potentially to very different degrees.

Likewise, all types of customers might be expected to be impacted, though again to different degrees.

***What scale of impact might be envisaged, and what drives it?***

Variations in impact for sellers can be expected to reflect, amongst other factors, different starting points (baselines) in different jurisdictions, the differences in types of conflicts of interest and possible mitigating measures across different jurisdictions and across different types of distribution models.

As set out above in section 7, national rules mean some sellers may already be subject to rules on conflicts of interest that are very close to those in MiFID. This is because the IMD is minimum harmonising and there is no EU harmonized regulatory standards applicable to insurance undertakings on conflicts of interest. This could include rules on direct sellers who do not fall within the scope of the IMD but where a Member State has imposed rules on insurance undertakings (direct sales). In addition, some sellers who undertake business that is subject to MiFID alongside their insurance business, may have elected themselves to apply the conflicts of interest policies they have for their MiFID

[15] See http://ec.europa.eu/internal_market/consultations/docs/2010/prips/costs_benefits_study_en.pdf, p. 27, fig 2.6 for an illustration. Derived from CEA data.

business across all their lines of business. For some sellers therefore, the closer the final measures are to existing national rules, the lower the impact.

Nevertheless, some sellers may be subject to rules on conflicts, but ones which are substantively different from those on MiFID. For other sellers, there may be no conflicts of interest measures in place currently. This would include those only selling insurance products who are not subject to national rules and who have not themselves elected to adopt conflicts of interest measures as part of normal good governance. For these two groups, impacts (costs) will be greater, as more extensive adjustments of organizational and administrative arrangements would be necessary. Arguably, benefits (if policy objectives are achieved) would also be greater.

For larger insurance distributors, it can be argued that it is more likely that seller will already have put in place some measures that address or manage conflicts of interest, as part of normal good governance and so as to manage potential reputational and operational risks. Some costs would therefore already be sunk. Since these measures may not align fully with those that might emerge under the changes examined here, there would however be adjustment costs. Smaller insurance sellers, including sole operators, might be expected to be less likely to have in place policies and measures on conflicts of interest. This needs to be taken into account, due to the fact that, in some jurisdictions, the number of insurance intermediaries who are natural persons is rather high.

From another perspective, absolute costs can generally be expected to scale with size.

One can anticipate that cost drivers include organisational changes and separation of functions, administrative and management costs, training and monitoring costs, impacts on product design and distribution. Costs can be split between one-off costs (implementation costs) and ongoing costs.[16]

Benefits for distributors could include, in principle, reduced mis-selling and associated redress and reputational impacts, and lower costs of complaints and, ultimately, improved business cases in view of more satisfied customers. Such benefits can be difficult to assess, as the inverse (consequences of poorly managed conflicts of interest) can also be difficult to estimate *ex ante*. For instance, the impacts of mis-selling scandals across whole sectors, due to significant retail market contagion, can see low probability events leading to very high negative impacts. There can be also specific contagion for insurance undertakings originating products, who can face liability for redress or

[16] A study by European Economics estimated one-off costs of change for implementing MiFID-style rules to be in the region of EUR 50 -125 million for intermediaries, and EUR 175-250 for insurance undertakings. For ongoing costs the respective figures are EUR 25-80 million and EUR 50-80 million. See http://ec.europa.eu/internal_market/consultations/docs/2010/prips/costs_benefits_study_en.pdf, p. vi and p. viii. However that study included all changes related to MiFID conduct of business rules, extending far beyond conflicts of interest, and the study noted that these estimates were subject to significant uncertainty.

reputational risk even where fault sits with distributors unconnected to the insurance undertaking.

Benefits for customers can be reasonably expected – if policy outcomes are achieved – to be driven most clearly through improved suitability of products for the demands and needs of the customer. This can have a major positive impact for individuals *in extremis*. However, in such conditions *in extremis* the impact can be very significant. The nature of possible impacts at the individual level can be conceptualised in terms of exposures to risks that the customer was not seeking to take, exposures to costs (and hence reduced performance) that were not understood, exposures to products with a maturity profile (liquidity) inconsistent with customer's potential demands and needs, or indeed opportunity costs – exposures to products that are not taking the risks and thereby exposed to the potential rewards, that the customer sought. All of these might see a misallocation of customer savings that harms the customer's best interests.

The potential extent to which different measures on conflicts of interest might carry benefits by reducing the potential for customer harm can be difficult to assess *ex ante*. For instance, purchases of investment products that do not match the demands and needs of the customer may only expose the customer to harm under certain stressed market conditions, or where the customer's circumstances change and early withdrawal is necessary. Aggregate impacts could be very significant given the size of the retail investment markets (the Commission estimates these to be around EUR 9 trillion across all sectors, with the UCITS and insurance-based investment markets roughly equal in scale and between them dwarfing other product types),[17] but it is difficult to isolate the contribution that conflicts of interest measures would have on their own. Further input from respondents to this Discussion Paper is sought.

There would be costs for customers also. A proportion of increased costs for insurance undertakings and insurance intermediaries would be passed on to customers, while there could be some impacts on choice and product range.

Note that consumer detriment linked to conflicts of interest may be significant at the level of the individual customer, irrespective of the size of the business engaged in the selling. A sole trader may cause harm as readily as a large undertaking, and *vice versa*.

The scale and nature of possible costs and benefits for different stakeholders related to different options in this work are not being quantified or assessed qualitatively at this stage. This section of this Discussion Paper is designed solely to gather views on the potential drivers of costs and benefits, and on the best ways for assessing their relative scale.

[17] See e.g. http://ec.europa.eu/internal_market/finservices-retail/docs/investment_products/20120703-impact-assessment_en.pdf, section 3.1, p. 10, p. 48.

*Note that many of these costs and benefits are driven by the changes at level one, rather than the possible changes at level two.*

***What would happen if no change was introduced?***

As already noted, in the absence of change one can surmise that unmitigated conflicts of interest could lead to harm for individual customers that would otherwise be avoided. Other measures – such as increased product oversight obligations for insurance undertakings and product intervention powers for supervisors, and improved product transparency measures (following the introduction of the KID) – might help reduce such harm.

Inconsistencies in regulation approaches at the EU level between sectors would continue, and could expose the insurance sector to stresses as a result of regulatory arbitrage. Other than the individual harm that might result from such stresses, this could lead also to reputational impacts across the whole sector by means of contagion.

A further factor is important. National measures can be expected to continue to evolve, including on conflicts of interest, leading to growing fragmentation of applicable standards across the EU, as different national regulators respond to issues in different ways, or different self-regulatory initiatives emerge in light of national specificities.

Such fragmentation could ultimately increase costs for at least some insurance undertakings, some insurance intermediaries, and indeed some customers.

**Questions on the impact assessment**

14. Are there other problem drivers that you believe should be considered?

15. Are there other entities or stakeholders who have not been identified here who could be impacted by changes?

    Please identify them and the nature and reasons for the possible impact, including is potential scale for them if possible.

16. Are there other drivers of costs or benefits that have not been identified?

    Please identify these drivers, and outline how their scale might be estimated, and which stakeholders they might impact.

17. Considering the differential impacts of changes for different stakeholders, are there other determinants for differential impacts that you would like to highlight?

18. How do you think effective estimates of costs and benefits for the different stakeholders impacted might be developed?

    Please consider in particular the challenges with estimating potential

benefits for customers and for the industry on an *ex ante* basis.

Please highlight any data sources you are aware of that might be used for developing such estimates.

## Annex 1

## MiFID II amendments to IMD

**Recital**

(87) Investments that involve contracts of insurance are often made available to customers as potential alternatives or substitutes to financial instruments subject to this Directive. To deliver consistent protection for retail clients and insure a level playing field between similar products, it is important that insurance-based investment products are subject to appropriate requirements. Whereas the investor protection requirements in this Directive should therefore be applied equally to those investments packaged under insurance contracts, their different market structures and product characteristics make it more appropriate that detailed requirements are set out in the ongoing review of Directive 2002/92/EC rather than setting them in this Directive. Future Union legislation regulating the activities of insurance intermediaries and insurance undertakings should thus appropriately ensure a consistent regulatory approach concerning the distribution of different financial products which satisfy similar investor needs and therefore raise comparable investor protection challenges. EIOPA and ESMA should work together to achieve as much consistency as possible in the conduct of business standards for these investment products. These new requirements for insurance-based investment products should be laid down in Directive 2002/92/EC.

(88) In order to align the rules pertaining to conflicts of interests, general principles and information to customers and to allow Member States to place restrictions on the remuneration of insurance intermediaries, Directive 2002/92/EC should be amended accordingly.

**Article 91**
**Amendments to Directive 2002/92/EC**

Directive 2002/92/EC is hereby amended as follows:

(1) Article 2(3) is amended as follows:

(a) the following point is added:

"For the purposes of Chapter III (A), "insurance-based investment product" means an insurance product which offers a maturity or surrender value and where that maturity or surrender value is wholly or partially exposed, directly or indirectly, to market fluctuations.

It shall not include:

(i) non-life insurance products as listed in Annex I of Directive 2009/138/EC (Classes of Non-life Insurance);
(ii) life insurance contracts where the benefits under the contract are payable only on death or in respect of incapacity due to injury, sickness or infirmity;
(iii) pension products which, under national law, are recognised as having the primary purpose of providing the investor with an income in retirement, and which entitles the investor to certain benefits;
(iv) officially recognised occupational pension schemes falling under the scope of Directive 2003/41/EC or Directive 2009/138/EC;

(v) individual pension products for which a financial contribution from the employer is required by national law and where the employer or the employee has no choice as to the pension product or provider.";

(b) the second subparagraph is replaced by the following:

"With the exception of Chapter III (A) of this Directive, those activities, when undertaken by an insurance undertaking or an employee of an insurance undertaking who is acting under the responsibility of the insurance undertaking shall not be considered as insurance mediation or distribution";

(3) after Chapter III, the following chapter is inserted:

"CHAPTER III(A)
ADDITIONAL CUSTOMER PROTECTION REQUIREMENTS IN RELATION TO INSURANCE-BASED INVESTMENT PRODUCTS

Article 13a Scope

Subject to the exception in the second sub-paragraph of Article 2(3), this Chapter applies additional requirements to insurance mediation activities and to direct sales carried out by insurance undertakings when they are carried out in relation to the sale of insurance-based investment products. These activities shall be referred to as insurance distribution activities.

Article 13b Prevention of conflicts of interest

An insurance intermediary or insurance undertaking shall maintain and operate effective organisational and administrative arrangements with a view to taking all reasonable steps designed to prevent conflicts of interest, as determined in Article 13c, from adversely affecting the interests of its customers.

Article 13 c Conflicts of interests

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

2. Where organisational or administrative arrangements made by the insurance intermediary or insurance undertaking in accordance with Article 13b to manage conflicts of interest are not sufficient to ensure, with reasonable confidence, that risks of damage to customer interests will be prevented, the insurance intermediary or insurance undertaking shall clearly disclose to the customer the general nature and/or sources of conflicts of interest before undertaking business on its behalf.

3. The Commission shall be empowered to adopt by means of delegated acts, in accordance with Article 13f, the following measures:

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

Article 13d General principles and information to customers

1. Member States shall ensure that, when carrying out insurance mediation distribution activities, an insurance intermediary or insurance undertaking acts honestly, fairly and professionally in accordance with the best interests of its customers.

2. All information, including marketing communications, addressed by the insurance intermediary or insurance undertaking to customers or potential customers shall be fair, clear and not misleading. Marketing communications shall be clearly identifiable as such.

3. Member States may prohibit the acceptance or receipt of fees, commissions or any monetary benefits paid or provided to insurance intermediaries or insurance undertakings, by any third party or a person acting on behalf of a third party in relation to the distribution of insurance-based investment products to customers.

Article 13e

The Commission shall be empowered to adopt delegated acts in accordance with Article 13f concerning Article 13c.

Article 13f Exercise of the delegation

1. The power to adopt a delegated act is conferred on the Commission subject to the conditions laid down in this Article.

2. The power to adopt a delegated act referred to in Article 13c shall be conferred on the Commission for an indeterminate period of time from ....

3. The delegation of powers referred to in Article 13c may be revoked at any time by the European Parliament or by the Council. A decision of revocation shall put an end to the delegation of the power specified in that decision. It shall take effect the day following the publication of the decision in the Official Journal of the European Union or at a later date specified therein. It shall not affect the validity of any delegated acts already in force.

4. As soon as it adopts a delegated act, the Commission shall notify it simultaneously to the European Parliament and to the Council.

5. A delegated act adopted pursuant to Article 13c shall enter into force only if no objection has been expressed either by the European Parliament or the Council within a period of three months of notification of that act to the European Parliament and the Council or if, before the expiry of that period, the European Parliament and the Council have both informed the Commission that they will not object. That period shall be extended by three months at the initiative of the European Parliament or the Council.

http://register.consilium.europa.eu/doc/srv?l=EN&t=PDF&f=ST%206406%202014%20ADD%201

## Annex 2

## CEIOPS Advice to the European Commission on the revision of the IMD

### "6.2.1 Possible conflicts of interest

1. There are various circumstances in which an insurance intermediary might encounter a conflict of interest, whether or not related to remuneration. This could be where his interest is in the outcome of a service provided to the customer, or a transaction carried out on behalf of the customer is distinct to that of the customer's. Non- exhaustive examples include:

a) intermediaries integrated in or part of an insurance group, which may represent a risk of their independence and impartiality in relation to the insurance undertakings integrated in the corporate structure;

b) incompatibilities where intermediaries who are also members of the governing bodies or fixed staff of an insurance or reinsurance undertaking; intermediaries who also exercise functions as appointed actuaries or auditors of insurance or reinsurance undertakings; intermediaries who also exercise functions as investigation experts of claims or claim adjusters or who are shareholders or members of the board of directors of a company that exercises that activity;

c) marketing or selling insurance products in association with the supply of other products or services (e.g. credit insurance offered by a bank associated to a loan), which is likely to enable the intermediary to make a financial gain at the expense of the customer (remuneration arbitrage);

d) contingent commissions, profit shares, volume over-riders, corporate hospitality and gifts, soft loans, training support;

e) reinsurance conflicts where placement of business is used to encourage insurers to use the intermediary to arrange reinsurance contracts, which trigger commission payments;

f) claims-handling and binding authorities: where the intermediary would not be able to act in the best interests of both customer and insurer, especially in the circumstances of a contested claim;

g) broker/agent: where an intermediary is both a broker (and thus representing interests of the insurance policy seekers) and an agent (representing the interests of insurers);

h) when an intermediary has a relative pursuing insurance intermediation or employed by an insurance undertaking; and

i) when an intermediary directly or indirectly receives a benefit from the loss settlement."

*Page 66*

https://eiopa.europa.eu/fileadmin/tx_dam/files/publications/submissionstotheec/20101111-CEIOPS-Advice-on-IMD-Revision.pdf

## Annex 3

## 3L3 Report on PRIPs

### "Annex 1: Possible model for PRIPs conflicts of interest

Level 1 requirements

1. PRIPs firms must take all reasonable steps to identify conflicts of interest between themselves and their investors or between one investor and another.

2. PRIPs firms must manage conflicts of interest in such a way to ensure, with reasonable confidence, that risks of damage to investor interests will be prevented.

3. Where the management of conflicts of interest cannot ensure, with reasonable confidence, that risks of damage to investor interests are prevented, PRIPs firms must disclose the general nature and/or sources of conflicts of interest to the investor before undertaking the business.

Level 2 requirements

4. PRIPs firms must establish, implement and maintain a conflicts of interest policy, set out in writing, that is appropriate to the size and organisation of the firm and the nature, scale and complexity of the conflicts of interest.

5. The policy must identify the conflicts of interest that may lead to a material risk of damage to the interests of one or more investors and must specify procedures to be followed and measures to be adopted to manage such conflicts.

6. Individuals engaged in the services that give rise to the conflicts of interest must carry on those activities at a level of independence appropriate to the size of the PRIPs firm and the materiality of the risk of damage to investors.

7. Effective procedures to manage conflicts include the following:

• measures to prevent or control the flow of information between relevant persons;

• the separate supervision of relevant persons;

• the removal of any direct link between remuneration or relevant persons engaged in the activity and the remuneration, or revenues generated by, different relevant persons engaged in another activity where a conflict of interests may arise;

• measures to prevent or control any person from exercising inappropriate influence over the way in which investment services are carried out; and

• measures to prevent or control the simultaneous or sequential involvement of a relevant person in separate services where such involvement may impair the proper management of conflicts of interest.

8. Disclosure of conflicts of interest must be made in durable medium and include sufficient detail, taking into account the nature of the investor, to enable the investor to take an informed decision with respect to the investment service in the context of which the conflict of interests arises.

9. A record must be kept of services in which a conflict of interests has arisen that has entailed a material risk of damage to the interests of one or more investors, or in which such damage may arise.

10. Common examples of potential conflicts of interest include:

- where a distributor has a holding, direct or indirect, representing more than 10% of the voting rights or of the capital in a given manufacturer;
- where a manufacturer or parent of a manufacturer has a holding, direct or indirect, representing more than 10% of the voting rights or of the capital in the distributor;
- the distributor is likely to make a financial gain, or avoid a financial loss, at the expense of the investor;
- the distributor has an interest in the outcome of a service provided to the investor or transaction carried out for the investor, that is different from the investor's interest in the outcome;
- the distributor has a financial interest or other incentive to favour the interest of another investor, or group of investors, over the interests of the investor;
- the distributor carries out the same business as the investor;
- the distributor will receive from another party other than the investor, an inducement in relation to the service provided, other than the standard commission or fee for that service;
- registration as an insurance intermediary in more than one category (with different levels of formal independence), or simultaneously as a reinsurance and insurance intermediary, which may give rise to arbitrary placement of insurance contracts. For example, broker/agent where an intermediary is both a broker (and thus representing interests of insurance policy seekers) and an agent (representing interests of insurers); or
- the distributor's interest in the insurance contract (e.g. in relation to which he is a beneficiary; occurring, for instance, in situations where a bank registered as an insurance intermediary is a beneficiary of a life insurance associated to a mortgage) potentially conflicting with the insured person's contractual interest."

*Page 39-40*

https://eiopa.europa.eu/fileadmin/tx_dam/files/publications/submissionstotheec/20101012-3L3-TF-Report-on-PRIPs.pdf

## Annex 4

**FORMAL REQUEST TO EIOPA FOR TECHNICAL ADVICE ON A POSSIBLE DELEGATED ACT CONCERNING DIRECTIVE 2002/92/EC ON INSURANCE MEDIATION, AS AMENDED BY AMENDED BY THE DIRECTIVE ON MARKETS IN FINANCIAL INSTRUMENTS REPEALING DIRECTIVE 2004/39/EC (MIFID (EC) NO XX/2014)**

With this mandate the Commission seeks EIOPA's technical advice to prepare a possible delegated act concerning the conflicts of interest provisions in insurance distribution activities, as laid down by Article 91 of the Directive on markets in financial instruments repealing Directive 2004/39/EC [MiFID] (the "MiFID II Directive"[18] also referred to as IMD 1.5 or the "legislative act"). Any such delegated act that may be proposed by the Commission must be adopted in accordance with Article 290 of the Treaty on the Functioning of the European Union (TFEU).

The Commission reserves the right to revise and/or supplement this formal mandate. The technical advice received on the basis of this mandate should not prejudge the Commission's final decision.

This mandate is based on Regulation No 1094/2010 of the European Parliament and the Council of 24 November 2010 establishing a European Insurance and Occupational Pensions Authority (the "EIOPA Regulation"), the Communication from the Commission to the European Parliament and the Council – Implementation of Article 290 of the Treaty on the Functioning of the European Union (the "290 Communication") and the Framework Agreement on Relations between the European Parliament and the European Commission (the Framework Agreement").

This request for technical advice will be made available on the DG Internal Market and Services website once it has been sent to EIOPA.

The mandate focuses on technical issues which follow from the MiFID II Directive. The following delegated act provided for by that Directive should be adopted so that it enters into application 30 months following the entry into force of the MiFID II Directive, taking into account the right of the European Parliament and the Council to object to a delegated act within 3 months (which can be extended by a further 3 months):

**According to Article 13c of the legislative act as laid down by Article 91 of Directive 2014/…/EC, the Commission may adopt by means of delegated acts the following measures:**

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

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

The European Parliament and the Council shall be duly informed about this mandate.

In accordance with the established practice within the Expert Group on Banking, Payments and Insurance, the Commission will continue, as appropriate, to consult experts appointed by the Member States in the preparation of this possible delegated act.

[18] The text referred to here is the text of the political agreement reached between the European Parliament and the Council revised by legal revisers and adopted by the European Parliament at the plenary session on 15 April 2014 but not yet published in the Official Journal. The text can be found at: XXX

The powers of the Commission to adopt a delegated act are subject to Articles 13(e) and (f) of the legislative act. As soon as the Commission adopts a delegated act, the Commission will notify it simultaneously to the European Parliament and the Council.

***

## 1. Context

### 1.1 Scope

The Insurance Mediation Directive[19] of 2002 (hereinafter "IMD1") lays down requirements on insurance intermediaries selling insurance products but not on direct selling of insurance products by insurers. The main objectives of the IMD review (hereinafter "IMD2"), proposed by the Commission on 3 July 2012 (COM (2012)360), are to enhance consumer protection and to achieve undistorted competition between all types of sellers of insurance products.

As the Council suspended discussions on IMD 2 in November 2012, the European Parliament, in the course of the MiFID II negotiations, requested that Chapter VII of the Commission proposal on IMD2 relating to *"Additional customer protection requirements in relation to insurance investment products"* was lifted from the proposal and brought forward and dealt with during the negotiations on the Commission proposal to recast Directive 2004/39/EC - COM (2011) 656 (hereinafter MiFID2). As a result of these negotiations, which were concluded on 14 January 2014, a new Article 91 was added in MiFID2, which amends IMD1 in respect of the sale of insurance-based investment products.

As regards IMD2, the European Parliament reached a position on 26 February 2014 and the Council will resume the discussion on 19 May 2014. It is hoped that under the Italian Presidency and the newly elected European Parliament the text can be finalized. This request for technical advice is written on the assumption that the relevant empowerment for the Commission on conflicts of interests, introduced by Article 91 of MiFID II, will be upheld during the IMD 2 negotiations.

### 1.2 Principles that EIOPA should take into account

In providing its technical advice EIOPA is invited to take account of the following principles:

- It should respect the requirements of the EIOPA Regulation.
- In accordance with the MiFID II Directive, EIOPA should work together with ESMA to achieve as much consistency as possible in the conduct of business standards for insurance-based investment products.
- Internal market: the need to ensure the proper functioning of the internal market and to improve the conditions of its functioning, in particular with regards to financial markets and insurance, and a high level of consumer protection.
- The principle of proportionality: the technical advice should not go beyond what is necessary to achieve the objective of the implementing acts set out in the legislative act.
- While preparing its advice, EIOPA should seek coherence within the regulatory framework of the Union, and in particular Commission Directive 2006/73/EC.

[19] Directive 2002/92/EC of 9 December 2002.

- In accordance with the EIOPA Regulation, EIOPA should not feel confined in its reflection to elements that it considers should be addressed by the delegated act but, if it finds it appropriate, it may indicate guidelines and recommendations that it believes should accompany the delegated act to better ensure their effectiveness.

- EIOPA will determine its own working methods depending on the content of the provisions being dealt with. Nevertheless, horizontal questions should be dealt with in such a way as to ensure coherence between different standards of work being carried out by the various expert groups.

- The provided technical advice should contain sufficient and detailed explanations for the assessment done, and be presented in an easily understandable language respecting current legal terminology at European level.

- EIOPA should justify its advice by identifying, where relevant, a range of technical options and undertaking evidenced assessment of the costs and benefits of each. The results of this assessment should be submitted alongside the advice to assist the Commission in preparing its impact assessment. Where administrative burdens and compliance costs on the side of the industry could be significant, EIOPA should where possible quantify these costs.

- EIOPA should provide sufficient factual data backing the analyses gathered during its assessment. To meet the objectives of this mandate, it is important that the presentation of the advice produced by EIOPA makes maximum use of the data gathered and enables all stakeholders to understand the overall impact of the possible delegated act.

- EIOPA should provide comprehensive technical analysis on the subject matters described below covered by the delegated powers included in the relevant provision of the legislative act, in the corresponding recitals as well as in the relevant Commission's request included in this mandate.

- The technical advice given by EIOPA to the Commission should not take the form of a legal text. However, EIOPA should provide the Commission with an "articulated" text which means a clear and structured text, accompanied by sufficient and detailed explanations for the advice given, and which is presented in an easily understandable language respecting current terminology in the Union.

- EIOPA should address to the Commission any question they might have concerning the clarification of the text of the legislative act, which they should consider of relevance to the preparation of EIOPA's technical advice.

## 2. Procedure

The Commission would like to request the technical advice of EIOPA in view of the preparation of the possible delegated act to be adopted pursuant to the legislative act and in particular regarding the questions referred to in section 3 of this formal mandate.

The Commission reserves the right to revise and/or supplement this formal mandate. The technical advice received on the basis of this mandate will not prejudge the Commission's final decision in any way.

In accordance with the established practice, the Commission may continue to consult experts appointed by the Member States in the preparation of the delegated act relating to the legislative act.

The Commission will duly inform the European Parliament and the Council about the final version of this mandate. As soon as the Commission adopts a possible delegated act, it will notify them simultaneously to the European Parliament and the Council.

**3. EIOPA is invited to provide technical advice on the following issues:**

**a) to define the steps that insurance intermediaries or insurance undertakings might reasonably be expected to take to (1) identify, (2) prevent, (3) manage and (4) disclose conflicts of interest when carrying out insurance distribution activities;**

The requirements on conflicts of interest foreseen by the MiFID II Directive (Article 91) cover a broad range of situations that may occur in insurance distribution activities. Insurance intermediaries and insurance undertakings are required to maintain and operate effective organisational and administrative arrangements with a view to taking all reasonable steps designed to prevent conflicts of interest as defined in Article 13b of the legislative act from adversely affecting the interests of customers (Article 13c of the legislative act).

Article 13c of the legislative act sets out the obligation for firms to take all appropriate steps to identify and to prevent or manage conflicts of interest. It appears that identification, prevention and management of conflicts of interest constitute the core requirements that insurance intermediaries or insurance undertakings must comply with while disclosure can only constitute a last resort measure and not a means for managing conflicts of interest.

Pursuant to Article 13c (3) the Commission is empowered to adopt a delegated act to further specify the appropriate steps insurance intermediaries and insurance undertakings are reasonably expected to take with respect to conflict of interests.

As regards remuneration, insurance intermediaries and insurance undertakings should take steps to identify, prevent, manage and disclose conflicts of interests when providing various investment and ancillary services, including those caused by the insurance intermediary's or insurance undertaking's own remuneration and other incentive structures.

The reception of third-party payments and benefits may influence insurance intermediaries and insurance undertakings in acting with the customer's best interests in mind, by incentivising them to recommend or sell a particular insurance-based investment product when another product may better meet the customer's needs. In order to strengthen the protection of customers and increase clarity as to the service they receive, conflicts of interest rules should take into consideration situations related to the reception of such third-party payments and benefits.

Certain investment products, such as insurance-based investment products, can be sold or distributed in different ways by insurance intermediaries or insurance undertakings. There are certain existing or potential conflicts of interests arising in the distribution of these products. These can be similar to the conflicts of interests found in the field of investments, but might have additional or different characteristics.

Therefore, EIOPA is invited to base its technical advice primarily on existing conflicts of interest rules, as laid down in Commission Directive 2006/73/EC, while at the same time ensuring regular consultation with ESMA as regards ESMA's work on its technical advice on Article 23 (4) (a) and (b) of MiFID II. In this respect, the EIOPA advice should be in line with the MiFID II Level 2 provisions as much as possible, in so far as it is consistent with IMD 1.5.

In particular, EIOPA is invited to consider the existing conflicts of interest framework under Commission Directive 2006/73/EC and to develop a similar framework for insurance intermediaries and insurance undertakings distributing insurance-based investment products. EIOPA should consider identifying remuneration or commission arrangements that lead to harm for the customers' interests and ways of avoiding these, or where

avoiding these is not possible, examine monitoring, or placing conditions or limitations on conduct and other arrangements that aim to limit harm to customers' interests.

In this context, EIOPA should also consider the framework for disclosure, including online disclosure, while identifying that disclosure is not a measure in itself to manage conflicts of interest. This should include how to devise content and how to ensure the quality of the information provided to customers in order to enable them to make an informed investment decision as regards insurance-based investment products.

EIOPA should also consider a requirement for periodical review of conflicts of interest policies or clarifications with respect to disclosure.

EIOPA is invited to consider in its technical advice the design of conflicts of interest frameworks to reflect the variety of the distribution channels that exist for the sale of insurance-based investment products. The size of firms carrying out the activity of insurance mediation should not alleviate responsibility on them from the obligation to devise a conflicts of interest policy.

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

With a view to establishing appropriate criteria for determining the types of conflict of interest whose existence may damage the interests of the customers or potential customers of insurance-based investment products, EIOPA is invited to verify to what extent the criteria in Directive 2006/73/EC need to be adapted and/or supplemented for insurance-based investment products.

Different products as well as different distribution channels might present different conflict of interest risks. EIOPA should also consider the timeframe of insurance-based investment products - notably what the conflict of interest issues are at the point of sale as well as during the products' lifetime.

EIOPA should consider that conflicts of interest are often related to the remuneration/inducements received by the insurance intermediary or insurance undertaking and therefore an essential element in designing the conflict of interest rules.

As the Directive establishes a similar framework for ESMA as regards conflicts of interest, EIOPA is invited to closely liaise with and consult ESMA when providing the technical advice to the Commission.

## 5. Indicative timetable

The delegated act on conflicts of interest in insurance distribution activities should enter into force at the same time as the delegated act on conflicts of interest in investment services. In order to achieve this it would be necessary for EIOPA and ESMA to work in parallel.

This target date should allow EIOPA sufficient time to prepare its technical advice for the Commission delegated act.

The deadlines set to EIOPA to deliver its technical advice are as follows:

| Deadline | Action |
|---|---|
| [June 2014 (estimated)] | Entry into force of the MiFID II Directive (the twentieth day following that of its publication in the Official Journal of the European Union). |

| | |
|---|---|
| 7 months after the entry into force | EIOPA provides its technical advice. |
| 6 months after the delivery of the technical advice by EIOPA (12 months after the entry into force of the MiFID II Directive)<br><br>At the latest 6 months after adoption by the Commission, deadline for the European Parliament and the Council to object (three months which can be extended by another three months) | Preparation, adoption of the delegated act and objection period for the European Parliament and the Council: In the preparation of the delegated act, the Commission will consult with experts appointed by the Member States within the Expert Group on banking, payments and insurance.<br><br>The Commission will provide the European Parliament with full information and documentation on those meetings. If so requested by Parliament, the Commission may also invite Parliament's experts to attend those meetings.<br><br>After adoption by the Commission of the delegated act and notification to the European Parliament and the Council, there is an objection period for the European Parliament and the Council (three months which can be extended by another three months). |
| At the latest 18 months following the entry into force of the MiFID II Directive | Publication in the Official Journal of the European Union (entry into force twenty days later). |
| 24 months following the entry into force of the MiFID II Directive | Date of transposition and publication by Member States. |
| 30 months following the entry into force of the MiFID II Directive | Date of application of the MiFID II Directive. |