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About BETTER FINANCE

BETTER FINANCE, the European Federation of Investors and Financial Services Users, is the public interest non-governmental organisation advocating and defending the interests of European citizens as financial services users at the European level to lawmakers and the public in order to promote research, information and training on investments, savings and personal finances. It is the one and only European-level organisation solely dedicated to the representation of individual investors, savers and other financial services users.

BETTER FINANCE acts as an independent financial expertise and advocacy centre to the direct benefit of European financial services users. Since the BETTER FINANCE constituency includes individual and small shareholders, fund and retail investors, savers, pension fund participants, life insurance policy holders, borrowers, and other stakeholders who are independent from the financial industry, it has the best interests of all European citizens at heart. As such its activities are supported by the European Union since 2012.

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INTRODUCTORY EXPLANATIONS (for non-professional readers)

European Union (EU) authorities aim to improve the conditions of saving and investing in capital markets for EU households through several regulatory and supervisory actions. Currently, most of these initiatives stem from the recommendations of the High-Level Forum on the Future of the Capital Markets Union,[1] on which the European Commission will follow-up with the *EU Strategy for Retail Investors*,[2] planned for the first half of 2022. This strategy aims to provide individual investors, among others, with adequate protection, bias-free advice, and transparent, comparable and understandable product information.

In preparation of its proposals, the EC tasked the European Supervisory Authorities in financial services (ESMA, EIOPA, EBA)[3] to provide technical advice on a range of topics. As such, EIOPA launched this public consultation to gather evidence and proposals from stakeholders on the topics and products that fall under its remit, i.e.:

- addressing and enhancing investor engagement with disclosures and drawing out the benefits of digital disclosures;
- assessing the risks and opportunities presented by new digital tools and channels;
- tackling damaging conflicts of interest in the sales process;
- promoting an affordable and efficient sales process; and
- assessing the impact of complexity in the retail investment product market.

In parallel, other calls for advice were sent to ESMA and EBA, to which BETTER FINANCE already responded.[4]

The products that fall under the remit of EIOPA, relevant for the EU Strategy for Retail Investors and the Capital Markets Union (CMU), are insurance-based investment products and occupational pensions.

Insurance-based investment products (IBIPs) are a mix between a typical insurance contract (providing coverage for an event) and an investment product (e.g. a mutual fund). Currently, life-insurances – one of the most sold type of IBIP across the EU – make for x% of EU households' financial savings.

IBIPs vary based on their specific purpose or functioning, but the most common categories are:

- unit-linked products, whose returns are *linked* to the performance of underlying investments (such as mutual funds);
- capital guaranteed products, which aim at protecting the value of the invested amounts (part of the insurance premium) in care of economic downturns;
- profit participation products, which enable the policyholder to share in the benefit of investments made by the insurance company; and
- hybrids, mixing characteristics of any of the above.

Occupational pensions include defined-benefit and defined-contribution plans. The type that is specific under the supervision of EIOPA are the *institutions for occupational retirement provision* (IORP), which is simply a legal form under which occupational pensions are organised, allowing them to be also distributed cross-border.

[1] HLF CMU Report 10 May 2022.

[2] EU Strategy for Retail Investors

[3] European Securities and Markets Authority (ESMA), European Insurance and Occupational Pensions Authority (EIOPA) and European Banking Authority (EBA).

[4]

General comment

BETTER FINANCE welcomes EIOPA's efforts to streamline and simplify information disclosed to consumers in financial services. We believe that the marginal utility of disclosures decreases as these grow in size and complexity, reaching a point from which these no longer deliver any benefits for individual, non-professional investors.

We find EIOPA's initiative particularly useful in light of the recent tendency of capital markets regulation to replace the liability of product manufacturers and intermediaries with consumer disclosures, which effectively shifts the responsibility on "retail" clients faced with biased distribution models and growingly complex products.

Essentially, BETTER FINANCE members share the view that, until a high level of financial literacy is achieved among financial services users, the latter are not equipped to deal with the current amount of information; on the contrary, research undertaken by BETTER FINANCE into information overload highlights that large and complex disclosures demotivate consumers from engaging and making informed decisions.

In this light, BETTER FINANCE very much welcomes two particular proposals of EIOPA (analysed in more detail under Q5 below):

- streamlining regulatory reporting requirements (the overlaps between applicable sectoral legislation); and
- identifying "vital information" that an investor should receive.

These are, indeed, the current two most efficient measures to be taken to improve the efficiency of disclosure documents for "retail" investors. In time, as financial education campaigns will start to show results, consumers will become more sophisticated and less dependent on intermediaries, which will prompt them to require more sophisticated information, as well as perhaps more detailed.

For the moment, we believe that EU sectoral legislation's pivot provision – client categorisation – should suffice to satisfy the information and product needs of more experienced and knowledgeable investors; the key aspect is to ensure that the criteria and procedure to disapply the general protection regime for "retail" clients are harmonised across markets.

Addressing and enhancing investor engagement with disclosures and drawing out the benefits of digital disclosures

Q1: What do you consider currently to be the most burdensome duplicative requirements between the different legislative frameworks? Do you consider there to be any duplicative disclosures which EIOPA have identified above between different legislative regimes to be not particularly burdensome for insurance undertakings or insurance intermediaries to comply.

We agree with EIOPA's proposals, and we believe that a few, factual information, such as the identities, contact details and addresses of insurance intermediaries are not particularly burdensome for consumers and can be kept (cf. tables 1 and 2, p. 12/13 of CP).

Q2. EIOPA can see some specific benefits in disapplying a number of disclosure requirements in the Solvency II Directive and the Distance Marketing of Consumer Financial Services Directive and rationalising any remaining requirements in the IDD. Do you agree with this approach?

To begin with, we find very useful the exercise undertaken by EIOPA to identify the duplicating disclosure requirements between the four applicable EU legislative acts. In our view, EIOPA's proposal to disapply or move consumer disclosure requirements from one legislative act to another amounts towards full consolidation, which will bring consistency and legal certainty.

The different mandated disclosures are, in fact, "heritages" of EU legislation adopted at different stages, which have not been coordinated one with another. In this sense, BETTER FINANCE generally agrees with the proposals set out in Table 1 of the consultation paper (p. 12-13).

However, these proposals would require legislative intervention from the co-legislators, reason for which we would find it more useful if EIOPA extended the reasoning behind the annual statement for IBIPs (paras. 53-83) to pre-contractual disclosures. Distinguishing between market transparency and supervisory purposes of disclosures, in comparison to consumer disclosures, is key in delivering optimal outcomes for non-professional investors. In this sense, as EIOPA correctly identified, there are certain information requirements in Solvency II or IDD that do not concern the consumer, reason for which it would be simpler if distributors and manufacturers would both: inform the client or prospective client of the existence of such information, leaving the choice to the former to access them or not; and maintain these records publicly accessible on the website, in an easy and consumer-friendly manner. Additional disclosures – of a general nature, concerning the product or the product manufacturer – should be available to consumers, but not disseminated, save where the consumer expressly opts for such disclosure.

However, there may be products distributed to clients that do not qualify as a PRIIP, reason for which eliminating entirely disclosure requirements from IDD on the basis of the existence of the PRIIP KID would create a blind spot for consumers. EIOPA should advise the European Commission to clearly distinguish the disclosure requirements for such products but, at the same time, aim to align as much as possible both the sequence and content with those of IBIPs. This links to the following question (Q3) and "pure protection" life insurances which are not IBIPs.

Q3. Notwithstanding the proposed approach set out in Q2, do you consider that there is an element of personalization under the provisions in Solvency II Directive that would justify delivery of personalized information separately and in addition to the generalized information in the PRIIPs KID?

In line with the answer provided for Q2, we agree with EIOPA's proposal to separate Solvency II disclosures for non-IBIPs, standardise them into a KID-like document, and move these requirements under IDD. It would bring significant benefits for consumer understanding, comparability, but also financial literacy, if such documents would be as similar as possible to the PRIIPs KID.

Q4. Do you agree that to address the current gap on periodic disclosures, it makes sense to require the disclosure of an "annual statement" which could include information on paid premiums, past performance, current value of the savings, as well as adjusted projections?

As mentioned in the earlier comments, we congratulate EIOPA for the progressive approach taken towards improving consumer disclosures. We believe EIOPA correctly identified, conceptually, the two pillars on which optimal disclosures for consumers rest and we advise EIOPA to coordinate with the other European Supervisory Authorities on this good practice: first, the need to make a distinction in EU law between disclosures as a tool for market transparency (derived from efficient market theories) and supervisory tools (capital market integrity and investor protection) and disclosure as tool to help consumers make an informed decision. However, we highlight in this sense that what consumers want to know may be very different from what consumers need to know, especially given the low level of financial literacy and behavioral biases consumers are prone to. In this sense, consumer disclosures must also have an educational dimension, to guide the consumer decision making towards the elements that underpin a sound and informed decision.

Second, we agree with EIOPA that the design of consumer disclosures must be based on behavioural testing, which must be done at Level 1.

In terms of what vital information should be subject to consumer testing, we believe that information on past performance should be added to the first layer in addition to the current value of savings (the savings "pot"). Moreover, as highlighted for Q12, the document should highlight whether ongoing commissions are paid or not to the distributor. In addition, given the current developments in terms of inflation, we believe that EU law should mandate the adjustment of net performance presentation with inflation, and standardise it across all consumer disclosures. Regarding the second and third layers performance and cost projections should be eliminated. In this sense, we believe that the readjustment of the performance projections will not have added value, but further confuse consumers.

Q5. Do you agree with the proposed list of "most vital" product and intermediary information? If not, what elements do you identify as being "most vital", that is essential information that is most critical for consumers to read?

Same answer as for Q4.

Q6. Do you currently see specific issues with misleading advertisements and marketing material in relation to the sale of insurance-based investment products (IBIPs), which would merit specific regulatory treatment and if so, which aspects?

In light of this question, BETTER FINANCE reiterates the concerns of its German member association defending the rights of insurance policyholders. They note a major concern with regard to interest rates published for IBIPs in advertisements and marketing materials, mainly because in most cases it is not highlighted that the interest rates apply to the net part of the insurance premium used for investment, not on the gross premium. They also note that entry and ongoing costs, as well as biometric risk costs strongly reduce the investment part of the gross premium (from 10% up to 40%). This obligation would significantly improve consumers' understanding of value for money delivered by IBIPs.

Assessing the risks and opportunities presented by new digital tools and channels

Q7. Do you agree on the current level of development of the market for online platforms distributing IBIPs? If not, please could you provide examples of where you see evidence of online platforms selling IBIPs at present and how you see this impacting the customer journey and if possible, any quantitative data you can provide on this distribution channel.

We agree with EIOPA's assessment of the market for online distribution of IBIPs, as well as the advantages and challenges presented.

Q8. Do you see the potential for the growth of open architecture models for the sale of IBIPs in the future and if so, in relation to which types of products?

We do not have additional evidence at local level on insurtechs, but we echo the position of our German member association on the growth potential of insurtech: first, most life insurance companies in Germany offer pension products and IBIPs through online channels; second, there are other growing business models in the area of IBIPs and pensions, including a future independent player for the PEPP.

Q9. Do you share EIOPA's assessment of the types of risks that could arise in the context of the growth of more diverse distribution channels for IBIPs? Are there any risks which you see arising, but which EIOPA has not identified in this paper?

In general, BETTER FINANCE agrees with the risks identified by EIOPA, but we wish to draw the attention also to the conclusions of the High Level Forum on the Future of the Capital Markets Union concerning *Open Finance* and to the fact that, particularly in the insurance industry, facilitating data exchange may pave the way to first or second degree price discrimination.

In our view, the first issue that must be tackled in opening access to data consumer data is enabling a real choice for consumers to agree or refuse. Given that insurances are, in most cases, legal obligations, concluding an insurance contract inherits the nature of an essential service for consumers. Thus, if an insurance intermediary subjects the conclusion of the insurance contract on the client's consent on data processing, that consumer no longer has a real, free (or unconstrained) choice on data processing.

Second, opening access to data must be subject to a levy on the insurance industry to enable EIOPA and national insurance supervisors expand their resources and adequately police practices that arise from a potential wave of data exchange. Given that insurance premiums are based on actuarial calculations, which heavily rely on data and information as statistical series, we believe that the highest risk of misuse and consumer detriment in open finance arises in the insurance industry, most notably via the potential first or second degree price discrimination for prospective policyholders.

Third, insurers must be obliged to be very transparent and upfront on how the data of consumers is used and if revenues are made from processing this data.

Last, open access must be strictly coordinated with the regulatory framework of the GDPR and in consultation with the European Data Protection Authority.

In spite of potential benefits that open access to data can bring, as it happened in the banking sector with payment services, we advise EIOPA to carefully examine a framework for open data that enables *safety by design* for consumers: prevention, rather than resolution, of consumer detriment is key in this field.

Tackling damaging conflicts of interest in the sales process

Q10. Do you agree with EIOPA's analysis of differences between IDD and MiFID II? Are there any other differences not mentioned which you consider to be relevant?

We agree with EIOPA's analysis and we believe it accurately reflects the differences between the two regulatory frameworks.

Q11. Do you have any views on EIOPA's analysis of the structure of different distribution models for the sale of IBIPs in the EU?

We agree with EIOPA on the analysis of the different distribution models for IBIPs, but we believe that quantitative data (market shares, types of underlying investments favoured, value of inducements, list of products for which commissions are received) would be very helpful in obtaining a clear picture of the market, both from a consumer and supervisory perspective.

Q12. Has EIOPA captured, in your view, all relevant policy options? Do you agree with the different pros and cons listed for these options and the potential impacts indicated for these options? Are you in favour of any particular options or combination of options? Are there any other policy options and pros and cons to be considered in your view?

BETTER FINANCE welcomes the assessment of EIOPA's different policy actions. We wish to highlight to EIOPA that, while none of the expressed actions would be a silver bullet, a package of the following could significantly improve the distribution channels of IBIPs and consolidate towards bias-free advice:

- *No.1: Refining existing rules in the IDD on inducements:*
- *No. 2: Further enhancing disclosure of inducements to consumers and making the concept of an "inducement" easier to understand for consumers:* we agree with EIOPA and believe that replacing the term of "inducement" with "sales commission" would be a clearer indication of their nature and more comprehensible for individual investors; in addition, EIOPA should require distributors to report the total amounts of inducements received on an annual basis and the entities from which these are received;
- *No. 3: Further bolstering rules on inducements at the product design phase ... and enhanced conduct supervision/enforcement by NCAs:* we reiterate the proposal of our German member in the sens that product design and the target market may be a cause of mis-selling. As such, we support EIOPA's proposal on reviewing the rules on the product approval process.
- *No. 4: Introducing a mandatory concept of "independent advice" into the IDD and introducing a ban on the payment/receipt of inducements for independent advice in line with MiFID II:* We fully support this proposal to the European Commission, which should

be embedded in the Level 1 legislation.

- *No. 5./6. Full ban on the payment/receipt of inducements and intermediate options:* We fully support a ban on execution-only services and/or a proposal for a cap on inducements.

Promoting an affordable and efficient sales process

Q13. Where do you see the most significant overlaps lie between the demands and need test and suitability assessment and what can be done to address these overlaps?

We believe that distributors should retain the obligation to assess the long-term needs of the prospective client as part of the suitability assessment. Also, in accordance with BdV, the most significant overlaps between the demands and needs test for execution-only services and the suitability assessment concerns biometric risk coverage, liquid reserves and the risk tolerance.

Q14. Do you see scope for streamlining the suitability assessment and in what way, could digitalisation be harnessed to make advice on IBIPs more affordable?

Yes, see answer to Q15 below.

Q15. Do you see any specific risks for consumers in streamlining the advice process further?

There are not other options to further simplify the advice framework. IBPs are considered as complex instrument with limited investment benefits (if the policyholder detain the contract until its maturity). Therefore, we consider that the assessment of target markets for these products should be kept. Most insurance policies underestimate the risk of biometrics and exaggerate the investment portion to raise premiums to be paid. In most cases, it is better to strictly separate biometric risk coverage (especially death and disability through separate policies) from long-term investment terms. these terms can be used for additional provisions. Indeed, IBIPs by their "product design" contradict this basic "best advice". Potential policyholders should therefore be at least aware of these two different aspects of "risk" (biometrics and investments) through their advice to be as "best" as possible.

Q16. What is your view on possible demand-side solutions to facilitate the provision of affordable advice on the sale of IBIPs and support wealth management, such as financial guidance and what benefits could this bring?

We believe that EU and national initiative on financial education are extremely useful. However, it should be pointed out that even a high level of financial education does not solve the problems of complex products. Indeed, the level of financial education will always be dependent to the level of education therefore there will be always a component of social conditions. at ESAs high-level conference on financial education and literacy of 01 February 2022, Aleksandra Maczynska, Executive Director of BETTER FINANCE underlined these considerations: https://www.eba.europa.eu/calendar/esas-high-level-conference-financial-education-and-literacy

Therefore, the best solution is providing a simpler palette of products together with affordable advice. for example Robo advisors can offer standardized, cost efficient and transparent products

(as for PEPP); although robo advisors as well need to be free of any bias component in the alghorytm or high commissioned IBIPs and controlled by independent institutions.

Assessing the impact of complexity in the retail investment product market

Q17. Do you agree with EIOPA's interpretation of complexity and cost efficiency in light of the changing market environment?

Based on input from our member organisations, there are several categories of IBIPs that can be regarded particularly complex, i.e. those that combine features that are difficult to understand by consumers, i.e. multi-option products combining biometric risk and capital markets risk, those that have opaque cost structures, and those with difficult to understand profit participation mechanisms.

Q18. Do you agree with EIOPA's assessment of the types of products and/or products features which could be considered simpler?

Yes, we agree with EIOPA's assessment. In addition, as mentioned by EIOPA, product complexity or simplicity is not dependent on the exposure to market risk, given that the guidelines on assessing complexity point, in fact, to the possibility of a consumer understanding the structure, cost, and risks of the product.

Q19. How would you, as an external stakeholder, define simpler and cost-efficient products? Could you please provide concrete examples of products that you consider simpler and cost-efficient?

BETTER FINANCE has supported and advocated the rationale behind the PEPP Regulation that such products should be "reasonably priced", to which we add that we also supported the introduction of the basic PEPP cost cap of 1%. The urgency of streamlining and making the IBIPs market more cost-efficient are underpinned by EIOPA's annual reports on cost and past performance, showing the ongoing damage the complex, fee-laden cost structures of IBIPs and pension product trigger for consumers.

As such, we believe that the basic PEPP should be taken as a starting point in defining "simple, cost-efficient and transparent" products, including IBIPs; other types of simple and cost-efficient packaged investment products concern both exchange-traded funds (ETFs) and/or clean share classes of mutual funds, which are cheaper than most of those used and distributed through life insurance wrappers.

Q20. Do you consider, as an external stakeholder, that other measures could be more effective in ensuring cost efficiency? Examples of such measures could include amending the wording of the POG Delegated Regulation and state more clearly that, in the product testing, manufacturers should also assess whether costs may be too high and hence not to fit for any target market.

In this sense, we draw to the conclusions put forward in EIOPA's consultation on value for money in the unit-linked insurance market, which should be extended to all types of IBIPs. Cost-efficiency, per se, can be argued in many cases by product manufacturers, but an adequate benchmark and additional references, amounting to value for money for consumers, are needed. Indeed, as identified by EIOPA, product manufacturers should *ensure by design* value for money for their customers, i.e. these assessments must start with the product approval process.

In addition, it is important how to assess the costs, and in this light we draw to our conclusions on the PRIIPs KID and the workstream from the PEPP KID on the inadequacy of the *reduction-in-yield* as a cost indicator. Should such an approach (of cost estimations) be preserved, we prefer the *Reduction-in-Wealth* proposed by BdV, which is used for the PEPP Benefit Statement.

Q21. Do you agree with the advantages and disadvantages of the different options proposed? Are there additional aspects which should be highlighted?

In light of this question, we wish to reflect the position of our member associations in terms of consumer concerns for complex products: there is a need for more guidance in terms of the redress measures (or other remedies for this purpose) that can be taken by consumers against the product manufacturer in case complex products are, in fact, sold to the unsuitable target market.

In other words, more emphasis should be put on the responsibility of product manufacturers to ensure that less complex products are designed and distributed, considering that consumers are not always in the position to properly evaluate such products and, thus, understand them. In addition, product complexity (as highlighted above) does not stem only from the risk evaluation in relation to securities markets (underlying investments and, thus, the investment dimension of the IBIP). In fact, as IBIPs are essentially insurance contracts, the mechanisms on pricing and covering biometric risks should also be more central to the assessment of complexity. In light of these arguments, we support Option 3 proposed by EIOPA (p. 89).

A ban of inducements would significantly improve the situation as the distributor would not be conflicted with other incentives to act in the best interest of the client and distribute products (either simple or complex) that are indeed suitable for the client.