



Packaged Retail Investment Products (PRIPs): New Ways of Thinking

Working Document by the Association of British Insurers

Introduction

1. The Association of British Insurers (ABI)¹ is the voice of the insurance and investment industry. Its members constitute over 90 per cent of the insurance market in the UK and 20 per cent across the EU. They control assets equivalent to a quarter of the UK's capital. They are the risk managers of the UK's economy and society. Through the ABI their voice is heard in Government and in public debate on insurance, savings, and investment matters. And through the ABI they come together to improve customers' experience of the industry, to raise standards of corporate governance in British business and to protect the public against crime. The ABI prides itself on thinking for tomorrow, providing solutions to policy challenges based on the industry's analysis and understanding of the risks we all face.

Key Messages

As work on the Packaged Retail Investment Products (PRIPs) dossier progresses, we call on the Commission to:

- remove remuneration bias from the sale of retail investment products;
- provide a regime where consumers can access high quality financial advice that is tailored to their specific needs;
- ensure that financial advisers and intermediaries provide high-quality advice when purchasing retail investment products; and
- ensure consumers are provided with clear, relevant and timely information enabling them to compare the key features of a range of different product types.

To achieve this, the ABI urges the Commission to:

- put the needs of consumers first when thinking about any new regulatory framework for PRIPs at a European level;
- recognise the importance of increasing consumers' savings and encouraging a competitive environment between different product types and manufacturers;
- focus on the economic purpose of a product, rather than its legal form – equivalent products should have equivalent regulatory treatment;
- recognise that consumers want, need and deserve a regulatory framework for selling practices that focuses on their needs, treats them fairly, enables them to understand the sales process and ensures that financial advice is not biased by remuneration arrangements with product providers;
- recognise that consumers want, need and deserve a regulatory framework for selling practices that focuses on providing timely, clear and relevant information that enables them to compare the key features of products; and
- co-ordinate work on PRIPs with the other Commission initiatives, including the reviews of the IMD, DMD and MiFID.

¹ The ABI's registration number on the European Commission's Register of Interest Representatives is: **730137075-36**.

Background

2. The market for PRIIPs is characterised by an enormous variety of products and providers – all competing for the savings of retail clients. A healthy and competitive market for PRIIPs has a key role to play in the recovery of Europe’s economies from the financial crisis. With trillions of Euros invested in PRIIPs, it is essential that consumers are confident that the market is operating effectively. The ABI believes that the PRIIPs project is an opportunity to ensure that Europe’s retail investors are well served by their providers and the market.
3. The Commission’s PRIIPs Communication in April asked a number of legitimate questions about the European market for PRIIPs. As major providers of PRIIPs in Europe, ABI members want to work closely with the Commission, MEPs and other stakeholders as the PRIIPs project progresses. We want any future European regime to be designed to improve investment outcomes for our customers and lead to increased confidence in our industry.

General Comments

4. It is essential to get the regime for PRIIPs right given the essential role these products play in the lives of citizens by providing easy access to financial markets. The financial crisis did not start in the retail savings market but savers have suffered from falls in asset values and their confidence has deteriorated. Consumer saving rises in a recession and if Europe is to take advantage of this, a framework is needed where product features are clearly and transparently explained to customers and products are sold fairly and with the interests of the consumer in mind.
5. Given the importance of PRIIPs as a channel for retail savings, the ABI is of the view that the Commission should seek to create a framework in which:
 - consumers have confidence in both the market and the individuals and firms operating within it. To achieve this, the market needs to be underpinned by a regulatory regime that requires product disclosures which ensure consumers understand the products they are purchasing. In addition, the rules on sales practices must ensure consumers are able to purchase the most appropriate product for their investment needs;
 - product providers operate under a regulatory regime that enables consumers to make effective provision for their medium and long-term financial needs. Demographic data suggests that Member States are increasingly facing challenges associated with an aging population. They alone will not be able to fund the future costs of long-term care or retirement provision. Consumers need to plan accordingly but most are either not saving for their retirement at all or are not saving at a rate that will provide them with sufficient retirement income. This means additional prescriptive regulatory burdens should not be placed on either consumers or product providers as these can increase the cost of PRIIPs at a time when consumers need to save as much as possible;
 - competition between products is encouraged. In a competitive market, product providers design products to assist consumers to achieve a return on their investment. Any regulatory intervention must continue to encourage product diversity and on-going innovation by product providers to respond to consumers’ evolving needs;
 - competition between product manufacturers must be encouraged. Complicated regulatory regimes lead to increased compliance costs which may act as a disincentive for firms to enter the market. This will reduce competition between firms, ultimately leading to higher costs for consumers; and

- the needs of consumers are the starting point. Although MiFID is undoubtedly the “benchmark” for rules on sales practices, it will shortly be reviewed. In our view, the Commission should adopt a “first principles” approach when designing any new framework. This means putting the work to date into a broader context where the question “how should the regulatory regime be designed?” is addressed rather than getting distracted by the current IMD or MiFID rules.
6. By using the principles outlined above to underpin any new regulatory framework, the European market for PRIPs will flourish to the benefit of both consumers and the industry. More consumers will gain access to, and have confidence in, the financial services industry generally and the insurance industry specifically. Without the confidence and trust of our customers, we recognise that we will not build a sustainable, innovative and profitable retail investment market. The ABI is committed to putting the needs of our consumers at the heart of all that we do. As a result, we have been considering how to improve retail investment outcomes for our customers. We are improving the clarity with which providers describe their services to their customers, removing remuneration bias from the advice process and increasing the professionalism of advisers. We call on the Commission to deliver a regulatory framework for PRIPs that supports us in achieving these goals.

Scope of PRIPs: Equivalent regulatory treatment for equivalent products

7. Getting the scope of the PRIPs project right is critically important. When considered from the perspective of the consumer, it is the economic function of the product that should decide its regulatory treatment and not the legal form in which it is packaged. All of the products under consideration in the PRIPs project have the same core economic function – they are investment products sold to retail investors. Therefore, we support the Commission’s proposed horizontal approach. This will facilitate consumers comparing between products and ensure that regulatory arbitrage does not drive sales. When considering products in the insurance family, unit-linked life products and with profits funds should clearly fall within the scope of the Commission’s work.
8. Other stakeholders have argued that “classical” or “traditional” life insurance products merit different treatment from other retail investment products and that they should not be included within the scope of the PRIPs project. The ABI does not support this view. From the perspective of the consumer, the economic function of these products is the same as any other retail investment product so they should be subject to the same disclosure and sales practice rules. The ABI is seriously concerned that arguments based on the “specificities” of particular products run a real risk of reinforcing, rather than replacing, the “sectoral patchwork” of regulation that currently exists at the European level, undermining the Single Market and leaving European consumers worse off.
9. Pension products share many features with PRIPs but the Commission will need to consider very carefully the implications of a decision to include pensions within the scope of PRIPs. Pensions policy is a key component of social and labour law which is a Member State competence. Indeed, pension products perform a fundamentally different public policy objective from other retail investment products meaning different regulatory considerations must be taken into account. If pension products are included within the scope of the PRIPs project, there is a real risk of disruption to the pensions market when the demographic challenges facing Member States means that consumers need to be offered every encouragement to save more.

Rules on selling practices

10. European consumers need and deserve a regulatory framework that focuses on their needs, treats them fairly and enables them to understand the sales process. The market must be underpinned by a regime that ensures consumers do not suffer detriment as a result of differences in selling practices between products. The MiFID regime is undoubtedly the “benchmark”. The ABI believes the Commission should focus on delivering a transparent sales regime for PRIPs; one that provides consumers with products that are appropriate for their financial needs, investment objectives and risk profile; and one that ensures that financial incentives from product providers do not influence the advice a consumer may receive. Below we have set out how we have been working to deliver these improved outcomes for our customers.

Providing advice to consumers

11. Not all consumers require advice when purchasing PRIPs. But where they do, consumers should be able to access high-quality and affordable advice that is tailored to their specific needs. We have been working on a model that will offer two different categories of advice:

- Independent Advice: This will be advice based on the financial adviser / intermediary undertaking a fair and comprehensive analysis of the relevant market. The advice will be unrestricted and unbiased because it will be free from the influence of any relationship between the adviser / intermediary and the product manufacturer; and
- Restricted Advice: This will be advice that considers the products available only in certain parts of the market, for example, only the products sold by a particular product manufacturer (tied or multi-tied advisers). The adviser will be required to disclose to the consumer at the outset any restrictions on the advice that they can offer. They must refer to themselves as a “restricted” adviser and explain to the consumer what that means.

12. In addition to new rules on advice, the ABI has developed a Simplified Advice Process (SAP). This new regime is likely to benefit low and middle income consumers with more straight-forward investment needs for whom an independent or restricted advice process is unnecessary or uneconomic. SAP will be a process driven solution designed to provide consumers with a personal recommendation after a consultation process, facilitated by the latest IT technology, lasting approximately 30 minutes. We are confident, on the basis of legal advice, that this regime is consistent with MiFID.

Professionalism of advisers

13. Ensuring that intermediaries provide high-quality advice is essential if consumers are to receive the advice they need when purchasing PRIPs. This means ensuring that those providing advice are qualified to do so. The ABI wants to see increased professionalism in the financial advice industry. If professionalism is increased, consumers should have greater confidence and trust in the financial services industry.

14. We want to see the Commission deliver a framework where all investment advisers are qualified to a higher minimum level than is currently the case; to be subject to a requirement for continuing professional development; and to abide by a code of ethics and standards of behaviour. This should be overseen by those with the power to hold advisers to account with sanctions for non-compliance. Those who fail to achieve the new qualifications standards or respect the ethics and values attached to new standards of behaviour should leave the financial advice industry. This is what consumers need.

Removing commission bias

15. Remuneration bias must be removed from the financial advice process because consumers deserve transparent disclosure of the remuneration arrangements of their advisers. If product providers offer commissions or inducements to advisers – whether they are tied agents or otherwise - to sell their products, it should not be a surprise that advisers will sell these products². The adviser has an inherent conflict of interest. The Commission’s Communication indicated a desire to see investors receiving “clear and effective disclosures of remuneration arrangements”. The ABI entirely agrees. Advisers should have a duty to act in their client’s best interests meaning bias of any form – and the perception of bias – must be removed from the sale of PRIPs. For the same reasons, product providers should not offer commissions or inducements to advisers.
16. By removing the bias inherent in the sale of PRIPs we would expect competition in the market to drive improvements in the products and services received by the end customer. By making product providers compete on the price and features of their products rather than the commission they pay to financial advisers, this should lead to increased consumer trust in financial services and the industry. An adviser should be able to decide the cost of their advice but this should not be set by the provider. The adviser should also be able to decide if their charge is conditional on the sale of a product but should explain how they charge at the beginning of a consultation and the client must agree. This will remove the perception that financial advice is a free service. It is not and nor should it be.
17. Such a radical change will not be without substantial costs to the insurance industry but this is an important investment that will deliver longer-term benefits for our industry and our customers. European consumers of PRIPs should enjoy the same transparency of disclosure and know that the advice they are receiving is not influenced by the commission an adviser or intermediary may receive.

Pre-contractual product disclosure

18. The ABI believes that improving communication with customers is an important part of improving consumers’ understanding of PRIPs. Providing information in a clear, relevant and timely way allows prospective customers to compare key product features, benefits and risks, and therefore understand whether the product is right for their needs.
19. In their Communication, the Commission indicated that the Key Investor Document (KID) currently being developed by the Committee of European Securities Regulators (CESR) under the UCITS IV Directive is the “benchmark” for improving product disclosure rules. We agree. Although not directly subject to the requirements of the UCITS Directive, the ABI has taken a keen interest in the proposals produced by CESR³ because it is important to get the framework right. The ABI also agrees with the Commission that the provision of appropriate information is essential to enable retail clients to compare products and to select those that are most suitable for their investment needs.
20. The ABI is committed to delivering improved information to our customers. Through industry driven initiatives, the ABI has sought to deliver improvements to the current projections and

² See for example:

http://www.crai.co.uk/uploadedFiles/RELATING_MATERIALS/Publications/Consultant_publications/files/pub_2634.pdf

³ See: <http://www.abi.org.uk/content/contentfilemanager.aspx?contentid=44192>

disclosure regime and we are currently undertaking research on the best way of disclosing to consumers the risks attached to particular products. The ABI's guidance for clear language and layout has helped our members review and develop customer focused projections and disclosure documents. Under the auspices of the industry-led Customer Impact Scheme⁴, the ABI has produced a number of guides to help our members deliver better communications for their customers.

21. It is important to recognise that providing effective product disclosure to consumers does not necessarily mean providing consumers with more information. Too much information is just as ineffective as too little information⁵. The focus needs to be on the quality of information rather than its quantity. Only by undertaking consumer research can the correct balance be found. In addition, excessively burdensome and prescriptive rules on product disclosure must be avoided as these have the potential to increase the cost of PRIPs for customers.

PRIPs: Must be co-ordinated with other Commission initiatives

22. The Commission has been undertaking a review of the DMD and has proposed reviews of both the IMD and MiFID in the near future. It is essential that work on the PRIPs project proceeds in parallel with on-going and contemplated European Commission initiatives. A holistic and co-ordinated approach is needed. If not, there is a real risk of overlapping and potentially inconsistent regulatory frameworks emerging at European level. This would impose unnecessary costs on financial services providers and create confusion for consumers, undermining the Commission's stated objectives. Therefore, we welcome the Commission's acknowledgement that any new legislative measures should effectively replace relevant existing measures.

⁴ See: <http://www.customerimpact.org/>

⁵ UK Better Regulation Executive and the National Consumer Council, *Warning: Too Much Information Can Harm*, November 2007.