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Insurance Policy
Financial Conduct Authority
25 The North Colonnade
Canary Wharf
London E14 5HS

23 November 2017

Dear Robert,

AFM Response to FCA consultation CP17/33, Insurance Distribution Directive, Implementation Paper 3

1. I am writing in response to this consultation paper, on behalf of the Association of Financial Mutuals. The objectives we seek from our response are to:

   - comment on the proposals, and highlight the need for further clarity in the way FCA intends to implement the proposals in the UK.

2. The Association of Financial Mutuals (AFM) represents insurance and healthcare providers that are owned by their customers, or which are established to serve a defined community (on a not-for-profit basis). Between them, mutual insurers manage the savings, pensions, protection and healthcare needs of over 30 million people in the UK and Ireland, collect annual premium income of £16.4 billion, and employ nearly 30,000 staff[1].

3. The nature of their ownership and the consequently lower prices, higher returns or better service that typically results, make mutuals accessible and attractive to consumers, and have been recognised by Parliament as worthy of continued support and promotion. In particular, FCA and PRA are required to analyse whether new rules impose any significantly different consequences for mutual businesses[2].

4. In addition, the Bank of England and Financial Services Act 2016 now provides an additional Diversity clause for FiSMA, to require the PRA and

[1] ICMIF, http://www.icmif.org/global-mutual-market-share-2013
[2] Financial Services Act 2012, section 138 K: http://www.legislation.gov.uk/ukpga/2012/21/section/24/enacted

FCA to take account of corporate diversity and the mutual business model in all aspects of their work[3].

5. We responded to FCA's first two consultations on IDD implementation, commenting on the very short timescales for firms to respond and act on FCA proposals, and calling for the regulator to be pragmatic in its expectations of firms in the first few months of the Directive taking effect[4]. We repeat that call again here, noting that FCA expects to need to consult further in December on some issues it had not finalising thinking on.

6. In our previous response, we commented at length on the problems some of our members were experiencing as a result of continued uncertainty over how FCA would interpret the grounds for products being defined as complex or not. In our view, the EIOPA guidelines on complexity published in October offers a clear assessment of the issue[5]. As we stated in response to CP17/23, in our view, "with-profits investment products with a maturity guarantee would ordinarily be regarded as non-complex". However, FCA's reluctance to address these issues has caused uncertainty in the market, and our members are preparing for IDD with different expectations of how (if at all) FCA will respond to those concerns. Where the market for regular premium with-profits endowments, and for Holloway contracts, are only today served by small friendly societies, the risk that has a materially different impact on mutual societies.

7. In our response to the second consultation and in a recent meeting with FCA, we also stated that in our view Holloway contracts, issued by a number of friendly societies, should not be classed as IBIPs. FCA confirmed that where a Holloway product was 'predominantly protection in nature' they should fall outside the definition of IBIP. By our assessment, all current Holloways would meet this criterion, assuming predominant means at least 50%, though it is critical for FCA to offer its own definition. For example, in the run-up to the RDR, AFM and FSA met on several occasions to explore this issue, and FSA develop a definition for 'Holloway lite', being products where less than 20% of premiums were directed to investment, which therefore fell into ICOBS.

8. A different group of our members are not-for-profit cash plan providers. These providers offer low cost health care products (with premiums starting from as little as £1 a week) and typically help less affluent people pay for dental and optical treatment, and for a wider range of health benefits. The incremental requirements in FCA's approach to implementing IDD are expected to add significantly to the cost of offering these products. Whilst for life companies the requirement to produce a KID closely mirrors existing disclosure rules (albeit with significant changes in places), the requirement for

[3] http://www.legislation.gov.uk/ukpga/2016/14/section/20/enacted

[4] Our responses are published on the AFM website:
http://www.financialmutuals.org/files/files/AFM%20response%20to%20consultation%20on%20IDD%20implementation%201.pdf; and
http://www.financialmutuals.org/files/files/AFM%20response%20to%20consultation%20on%20IDD%20implementation%2C%20paper%202.pdf

[5] https://eiopa.europa.eu/Publications/Reports/Final_Report_IDD_guidelines_execution_only.pdf

an IPID and demands and needs statement for non-life policies breaks new ground. In our view there is still a high degree of uncertainty on the content and expected treatment of these documents. For example:

a. in CP17/7, FCA states the demands and needs statement should be issued before the end of the contract. CP17/23 makes a similar requirement for the IPID. As many cash plan products are largely written on a monthly renewable basis, the definition of contract used by cash plan providers relates to the period before the application process is complete. For other non-life insurers, the term "end of the contract" would coincide with the termination of cover: therefore, the effect on annually renewed products is quite different from products written on a short-term basis (such as cash plans or immediate travel cover for a one-week holiday). FCA indicates it is for firms to determine themselves when to issue these documents, but greater clarity would be helpful;
b. many cash plan products are sold on a group basis, as a free benefit provided from the employer. Traditionally therefore there is no underwriting process, and a master policy is issued to the employer; hence, the individual employee might only receive policy literature if they upgrade cover. Producing a tailored demands and needs statement to the individual might be problematic, as cover is provided on a standard basis. Equally, the need to provide an IPID to the individual (as our members have interpreted) would require a complete new element in the sales process and prove very costly. This is not covered in the consultation papers so far.

9. We recognise that as a result of the slowly evolving detail from EIOPA, and FCA's own publishing deadlines, there have been overlap between publications, and some material has been written in haste. As a general reflection of the consultation therefore, we have found the latest consultation has not been as clearly written as most FCA papers. Indeed, with the overlap of papers and the need to balance existing and extensive FCA rules against the requirements of the IDD, we consider the coverage in this consultation is most clear when FCA has simply copied across the EIOPA text. To illustrate, many of the chapters in the consultation do little more than signpost the draft rules, with very little explanation, and the 200 pages of appendix are not clearly laid out (for example, draft rulebook sections follow neither the order of the consultation, nor alphabetical order, nor the order of the existing FCA sourcebooks). Further, draft rules are not page referenced from the consultation text, giving the impression that multiple authors have cut and paste material together without any consideration of the clarity of the whole.

10. For these reasons and the generally unsatisfactory process adopted to implementation of the IDD in Europe, we consider FCA should strongly echo the calls already being made in the European Commission for a delay to the introduction of the Directive. Should there be a decision to delay, there becomes a doubt whether the IDD will be incorporated before the UK leaves the European Union.

11. Whilst we recognise the UK is subject to EU directives until March 2019, we also note that in other countries the national supervisors have not been as rigorous in implementing new directive requirements as we have in the UK, and would ask FCA to explore with Treasury whether a delay to the timetable of even a few months, raises the opportunity for the UK to avoid implementation at all. As stated in paragraph 10.5, one of the purposes of the IDD is "to ensure there is an effective single market for insurance distribution activities". Currently it is unclear whether that will be achievable once the UK leaves the EU, at least "without requiring additional authorisation".

12. Our responses to specific questions raised in the consultation are attached below. We would welcome the opportunity to discuss further the issues raised by our response.

Yours sincerely,

Chief Executive
Association of Financial Mutuals

Our responses to specific questions raised in the consultation

Q1: Do you agree with our proposal to reproduce the POG and IDD regulations in the Handbook, and to apply the provisions of the draft regulations as rules to a wider range of firms?

We agree with the intent. FCA accepts that reproducing the draft POG and IDD regulation (and to reflect draft UK legislation) into the Handbook, before they are finalised, may require further consultation, and in turn produce uncertainty and complication. However, firms face unrealistic timescales for implementing IDD, so anything that can be done to ensure they can plan with greater certainty, is helpful.

Q2: Do you agree with our further proposals in relation to the inducements requirements for IBIPs? Where possible, please distinguish between the minimum IDD requirements and areas where we have exercised discretion.

The proposals are intended to retain a level playing field between products covered by the IDD and MiFID2. These are products which are generally seen as interchangeable for regulatory purposes, though in reality many consumers would not regard them as substitutable. It is unfortunate that the treatment between this consultation and CP17/23 means that in order to read the proposed rules it is necessary to view both and cross-refer, even where the proposals in CP17/23 are not yet made rules, and to have an understanding of MiFID requirements as well as IDD. This complicates the process and risks transcription errors.

Q3: Do you agree with our proposals in relation to the suitability and appropriateness requirements of the IDD Regulation?

We agree, though we note in paragraph 5.7 that FCA accepts IBIPs created under IDD may be at a competitive disadvantage compared to MiFID 2 products, where firms issuing the latter are permitted to assume professional clients have the necessary knowledge and experience, but where this is not applied to products under IDD. One option not discussed in the paper is whether FCA should amend the MiFID related rules where it is prevented doing so for IDD regulations, to ensure a level playing field.

Q4: Do you agree with our proposals for introducing new rules to retain existing disclosure requirements for life policies?

We agree.

Q5: Do you agree with our proposal to include guidance to clarify the meaning of 'in good time'?

The text both in the consultation and in the draft rules is very vague and only offers an arbitrary sense which presumably requires a firm to determine for itself what 'in good time' means in the context of each customer and each transaction. Whilst we recognise FCA would wish to encourage firms to provide appropriate timescales, we consider FCA might have provided some examples of good practice.

Q6: Do you agree with our approach to implementing the IDD disclosure requirements in relation to mandatory occupational pension schemes?

Q7: Do you have any information regarding the availability or potential future availability of mandatory occupational pension schemes based on an insurance contract in the UK?

These issues are outside the scope of our members, and we offer no comments.

Q8: Do you agree with our proposals in relation to conflicts of interest including our approach for the requirements of the IDD Regulation? Where possible, please distinguish between our proposals in respect of the minimum directive requirements and areas where we have exercised discretion.

This section of the consultation appears to have been written in haste, and both the commentary and draft rules are not clearly laid out. For example, some of the formatting is wrong, and the reference in paragraph 7.6 to SYSC 10.1.4R(4) appears to refer to another clause, and the use of negative clause numbers reinforces the appearance of unclear presentation.

That said, our interpretation of the draft rules is that they are consistent with the IDD regulations and we agree with the intent.

Q9: Do you agree with our proposed approach to product oversight and governance rules including:

a. *the approach in relation to the POG Regulation*
b. *retaining current guidance under the RPPD*
c. *introducing new provisions based on MiFID PROD requirements?*

We agree with the approach in relation to the POG regulation and on retaining current RPPD guidance. These provide a high-level and familiar structure for product oversight.

As we stated in our response to CP17/23, we were concerned that FCA proposed to extend requirements from MIFID to all insurers. Whilst there is an argument for levelling the playing field between MiFID-products and IBIPs, that certainly does not apply for non-life insurance. We therefore feel that the proposals go beyond those intended by IDD for general insurance and health products. FCA has not presented a strong case for

extending the directive requirements, and the effect is clear in the (limited) evidence presented in the cost benefit analysis. This shows average one-off and ongoing costs for general insurers of £139,000 and £230,000 respectively; this compares to figures for life providers of £11,000 and £0.

This is explained in part by the extra sequences in the administrative process that are added for a non-life insurer. Where historically FCA has determined that the disclosure process in the UK largely works effectively, this suggests products like health cash plans suffer from the unintended consequences of issues elsewhere. Where cash plan premiums can start from as little as £1 a week, the extra costs provided in FCA's cost benefit analysis produce a renewed risk that providers will be forced out of the market.

And as these products are frequently purchased by the less affluent, and where there are no close substitutes, this would increase the risks of financial vulnerability. Equally, where cash plans are operated on a not-for-profit basis, and where their profits are reinvested into local communities, there would be wider unwelcome consequences for society.

We accept that the sample size was unhelpfully small, and are not aware of any members of AFM that were requested to support the data survey, so we cannot comment on the accuracy and relevance of these numbers. However, it is undeniably the case that the greater burden falls on non-life manufacturers, and this is a significant concern to our members who tend to be small and would therefore have to reassess pricing to take account of the extra regulatory costs imposed.

The benefits posted by FCA focus mainly on PPI mis-selling. As almost all fines and redress for inappropriate sales of PPI have been levied against deposit-takers, and are not directly in scope of the IDD, this is unhelpful and potentially misleading.

We suggest FCA simplifies the requirements for non-life companies, given evidence from its own reviews that there is less risk of consumer detriment for these products.

FCA's contention that its proposals "have no significantly different impact on mutual societies" is, in our assessment wrong, both in relation to cash plans, but also as described above for smaller with-profits mutuals.

We note that PROD 4.4.4 G (2) includes a reference to provider, which conflicts with the use of the term manufacturer elsewhere in these proposals.

Q10: Do you have any comments on the draft Perimeter Guidance?

Chapter 9 briefly sets out the approach taken by FCA to changes in PERG. We note that in several places FCA proposes to maintain rules that go beyond the requirements of the IDD, though the text in the consultation paper does not set the reasons for this in detail. The language in the chapter mainly replicates the technical detail in the draft rules, and we would have preferred a greater effort from FCA to adopt clearer language and less opaque description.

For example, the definition of remuneration in PERG extends beyond that of IDD, by retaining existing rules on top of the IDD, but without explaining the benefit to consumers.

We also note that the layout and clarity of some paragraphs in the draft rules could be improved: see PERG 5.6.4E as an example, where there are at least two typing errors.

Q11: Do you have any comments on our proposed approach to implementation of the IDD requirements in relation to registration?

The approach appears valid, though we note that the arrangements are subject to further consultation in December, and that this will put further pressure on firms to be ready for implementation of the rules.

Q12: Do you agree with our proposed Handbook changes on passporting?

We agree.

Q13: Do you have any comments on our proposed approach to amend PROF and the application of the handbook for authorised professional firms?

No comments.

Q14: Do you agree with our proposed changes to the Handbook modules in paragraph 11.3?

We agree.

Q15: Do you agree with our proposal to incorporate the requirement of Article 10(8) of the IDD into SYSC?

We agree.