



THE SOCIETY OF ACTUARIES IN IRELAND

**Submission on the Central Bank of Ireland's
Second Consultation on
Review of Consumer Protection Code**

July 2011

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1 Introduction

- 1.1 The Society of Actuaries in Ireland is the professional body representing the actuarial profession in Ireland. Many of our members hold responsible roles within, or as advisers to, financial services firms. They act as board members, Appointed Actuaries (with statutory responsibilities), Signing Actuaries (also with statutory responsibilities), and senior managers carrying a range of responsibilities including financial and risk management.
- 1.2 In addition, the Society is an active member of the Groupe Consultatif Actuariel Européen and is fully engaged in the Groupe's ongoing work on governance systems and prudential regulatory standards, especially in relation to the development of Solvency II.
- 1.3 The Society seeks to make an impartial contribution to public debate on social policy and public interest matters where our members' knowledge of the financial services industry can add value. In this context, we welcome the opportunity to submit this response to the Central Bank of Ireland's Consultation Paper 54 (CP54), "Second Consultation on Review of Consumer Protection Code".
- 1.4 We support the Central Bank's continued objective to strengthen the consumer protection framework. We welcome the introduction of revised measures which will benefit consumers in their dealings with the financial services industry and which will provide both additional protections and enhancements to existing provisions.
- 1.5 In preparing this response, we have primarily focused on areas where we feel the revised Consumer Protection Code (the "Code") is not meeting this objective. In particular, we have commented on areas where compliance with the Code will result in providing consumers with much additional information that is of potentially limited benefit and may serve to obscure more important or relevant information. We have also commented on aspects of the Code that may be unworkable, confusing, inconsistent or potentially detrimental to consumers' interests.
- 1.6 We provide general comments in Section 2, followed, in Section 3, by responses to some of the specific issues on which comments were invited in the consultation paper. The Society responded to Consultation Paper 47 (CP47), "Review of the Consumer Protection Code". Many of our comments in Section 2 reflect our responses to questions 11 to 14 posed in CP47. For this reason, we have included our responses to questions 11 to 14 of CP47 in Appendix A of this submission.

2 General Comments

2.1 In this section we comment on the following aspects of the new Consumer Protection Code provided in CP54:

- Product Producer Responsibilities
- Information about products – terms & conditions
- Investment Products
- Information about charges
- Statements – Investment Products.

Product Producer Responsibilities

Provisions 3.46 to 3.50

2.2 We believe a technical definition of the terms ‘intermediary’ and ‘intermediary channel’, as used in Provisions 3.46 to 3.50, should be included in the Code. For example, it is not clear if the term ‘intermediary’ is intended to include sales employees, tied insurance agents for whose actions the insurer has taken full and unconditional responsibility, and tied insurance agents for whose actions the insurer has not taken full and unconditional responsibility.

Provision 3.47

2.3 CP54 defines the Target Market as “the profile of the group of consumers at which the regulated entity aims a particular investment product”. This definition of Target Market could be interpreted as the business decision of the regulated entity to target a particular group of consumers. This will change from time to time depending on factors such as the size of the market, product profitability, distribution channels available, the intermediary’s ability to sell the appropriate products to the chosen market, and the corporate strategy.

2.4 We believe the definition of target market should relate to the types of consumers for whom the product is likely to be suitable, using criteria such as:

- investment objectives
- time horizon
- attitude to risk
- level of investment knowledge & experience.

We expand on the above criteria under our response to question 11 of CP47 (Appendix A).

Provision 3.48.

- 2.5 We note that the following sentence has been added to the end of this Provision: “The information must be provided in plain English”. “Plain English” is an exacting and ill-defined requirement. In some cases, the absolute use of “plain English” and the complete avoidance of industry terminology is not possible where adequate information needs to be provided on complex products.
- 2.6 In this regard, we would point to the UCITS IV Key Investor Information requirement for ‘presentation and language’ as a possible standard to be achieved:

“... clearly expressed and written in language that communicates in a way that facilitates the investor’s understanding of the information being communicated, in particular where:

(i) the language used is clear, succinct and comprehensible;

(ii) the use of jargon is avoided;

(iii) technical terms are avoided when everyday words can be used instead”¹

In addition, the Committee of European Securities Regulators (CESR) – now the European Securities and Markets Authority (ESMA) - has produced a guide to clear language and layout for the UCITS Key Investor document.²

- 2.7 For the reasons given in paragraph 2.5, we consider that the last sentence of Provision 3.48 should be deleted. The Provision could be expanded upon as outlined in paragraph 2.6 if it is considered necessary to further clarify the requirement to provide clear information.

Provision 3.50

- 2.8 We consider that the revised wording of Provision 3.50, “Where the **product producer** establishes that the **target market** of **consumers** for the **investment product** has changed, the **product producer** must . . .”, is not consistent with the new definition of Target Market (“the profile of the group of **consumers** at which the **regulated entity** aims a particular **investment product**”). The definition implies that the Target Market is within the control of the regulated entity, i.e. a business decision, whereas the above text of Provision 3.50 implies that it is outside the control of the entity.
- 2.9 We consider that the corresponding wording in CP47 - “Within the first year of launching an **investment product**, and annually thereafter, a product producer must check whether the product is continuing to meet the general needs of the target market for which it was designed. Where the product producer establishes that a product no longer meets the general needs of the target market, the product producer must: ...” - is clearer and more constructive than the new wording of Provision 3.50.

¹ Commission Regulation (EU) No 583/2010 (http://ec.europa.eu/internal_market/investment/ucits_directive_en.htm)

² “CESR’s guide to clear language and layout for the Key Investor Information document”

(http://bit.ly/ESMA_10_1320)

- 2.10 With respect to updating the information required under Provision 3.47, we believe that each product should have specified triggers, defined by the product producer, that require an immediate review. For example, for tracker bonds, a downgrade of a counterparty should automatically trigger a review.
- 2.11 We consider that clause (b), to notify the Central Bank, requires further elaboration. What details are required? How soon is notification required? What action will the Central Bank take on such notification, if any?

Information about products – terms & conditions

Provision 4.26

- 2.12 In relation to Provision 4.26, we note the requirement to provide customers with a copy of “the terms and conditions attaching to a product or service” before they enter into that contract or service. CP47 specified that this must be provided “before entering a contract or before the cooling-off period expires”.
- 2.13 In the context of Provision 4.26, we assume that “terms and conditions” does not refer to the full policy document or terms and conditions of a life insurance or pension plan, which in many cases would be a very lengthy document. Similarly, we assume that the information currently provided in the Customer Information Notice under the Life Assurance (Provision of Information) Regulations, 2001 meets this requirement. However, we suggest that “terms and conditions” in Provision 4.26 be defined or clarified. Alternatively, we suggest that the reference to the cooling-off period in CP47 be restored.

Investment Products

Provision 4.62

- 2.14 Extract:

“4.62 Before offering, arranging or recommending an *investment product* the *regulated entity* must provide the *consumer* with the following information, where relevant, in a stand-alone document:

- a) capital security;
- b) the risk that some or all of the investment may be lost;
- c) leverage and its effects;
- d) any limitations on the sale or disposal of the product;
- e) restrictions on access to funds invested;
- f) restrictions on the redemption of the product;
- g) the impact, including the cost, of exiting the product early;
- h) the minimum recommended investment period;
- i) the risk that the estimated or anticipated return will not be achieved;
- j) the potential volatility in price, fluctuation in interest rates, and/or movements in exchange rates on the value of the investment; and
- k) the level, nature, extent and limitations of any guarantee and the name of the guarantor.”

- 2.15 We note that the leading sentence of the corresponding section in CP47 stated (emphasis added): “...must provide the consumer, where relevant, with information about: ...” - as distinct from (emphasis added) “must provide the consumer with the following information” in the CP54 text.
- 2.16 In addition, we note that bullet “j” in CP47 states “...the potential effects of volatility...” as distinct from CP54 which states “...the potential volatility...”.
- 2.17 While it is possible to provide information about risks and about the potential effects of volatility and fluctuation in interest rates, it is not possible to definitively state risks or potential volatility/ interest rate fluctuations in absolute terms, as a literal reading of the modified wording in CP54 requires. Similarly, the requirement to “provide the *consumer* with . . . movements in exchange rates on the value of the investment” does not make sense – the requirement should be to provide information on the effects of movements in exchange rates.
- 2.18 We believe that the wording for the above reference parts of Provision 4.62 should revert to the text of CP47.
- 2.19 As several of the information categories listed under Provision 4.62 are currently provided to the consumer under the Life Assurance (Provision of Information) Regulations 2001 or other regulations, we suggest that the last paragraph of this provision be replaced with: “Where the information required by Provision 4.62 is already provided to the consumer under the Life Assurance (Provision of Information) Regulations 2001 or any other regulations made under Section 43D of the Insurance Act 1989 requiring the provision of information to consumers regarding life assurance policies, the regulated entity is not obliged to include that information in this document.”
- 2.20 Similarly, we believe that the regulated entity should not be obliged to include information relating to PRSAs (or Occupational Pensions) that is already provided to the consumer under the corresponding disclosure regulations (Personal Retirement Savings Accounts (Disclosure) Regulations, 2002 / Occupational Pension Schemes (Disclosure of Information) Regulations, 2006).

Information about charges

Provision 4.72

- 2.21 We believe it would be helpful to clarify if the requirement to provide a written breakdown of all charges under Provision 4.72 (a) is met by the information currently provided under the Life Assurance (Provision of Information) Regulations, 2001.

Statements – Investment Products

Provision 6.5

- 2.22 In relation to Provision 6.5 we assume that when providing the information required on a forecast basis, it is sufficient to provide information consistent with that needed to populate the "Illustrative Table of Projected Benefits and Charges" table as required by the Life Assurance (Provision of Information) Regulations, 2001. We suggest that Provision 6.5 should be clarified in this regard.

3 Response to Section 2 of CP54

3.1 In this section, we comment on some of the specific areas identified within Section 2 of CP54. The heading numbers below correspond to heading numbers in Section 2 of the paper.

iii) Unsolicited Contact

Provisions 3.31 and 3.32

3.2 The current Consumer Protection Code, and CP47, include an exemption whereby insurers may make unsolicited contact with existing or potential customers for the purpose of offering protection policies. We believe that the removal of this exemption, as proposed in CP54, is likely to have unintended consequences, particularly in relation to life assurance.

3.3 It is widely acknowledged that life assurance needs to be proactively sold – for many consumers, it is not a product that they would seek out under their own initiative. Yet it is a product that serves a real need for most consumers. If the exemption for protection policies is removed, there is a risk that elements of the market, particularly lower socioeconomic groups, will be underserved in this regard.

3.4 The change will impact on insurers' ability to market to certain target segments and may lead some companies to review their participation in the market in general. This could lead to a reduction in competition and this would ultimately not be in consumers' interests.

vi) Advertising

3.5 With respect to Chapter 9, we would caution that a balance must be maintained between ensuring the consumer is fully aware of the risks involved and ensuring the consumer is not confronted with so many warnings that he or she finds it difficult to process the key information.

Provisions 9.34 to 9.54

3.6 In Chapter 9, Provisions 9.34 to 9.54 are categorized under the heading "Investments". This categorization is not consistent with the term "Investment product" used elsewhere in the Code and defined under Definitions in Chapter 12. It is therefore unclear to which products Provisions 9.34 to 9.54 apply.

3.7 We consider that there are a number of difficulties with Provision 9.34 as follows:

- It is not clear how the variable [xx%] is to be calculated or determined in the case of open ended collective investment funds with no guarantee. Inserting 100% for xx% as a default in such cases is an extreme measure. Also, the potential [xx%] loss does not reflect the risk profile of a fund. For some funds, by the nature of their underlying investments, the risk of 100% loss is extremely remote, e.g. a fund investing in short dated bonds. We note that Provision 4.62 (b) requires a statement of the risk that some or all of the investment may be lost. This may be a more balanced and consistent way of conveying Provision 9.34.

- There are investment products which offer a money back guarantee, but where the guarantee is provided by a counterparty. Under such a product, the consumer is exposed to counterparty risk. The consumer could therefore lose 100% of his or her capital invested in such a product if the counterparty defaults. However, such a product would not be subject to Provision 9.34 on the basis that the product appears to offer a guarantee of 100% of the capital invested.
- The measure does not distinguish or refer to the duration at which a product may offer a guarantee of 100% of capital. For example, if a collective investment fund offers a money back guarantee in, say, 20 years' time, it then falls outside Provision 9.34, even though such a guarantee is of little practical value to a consumer with a shorter investment horizon.
- It is unclear if the Provision relates only to single premium investment products or also to regular savings plans.

We believe that Provision 9.34 is therefore unfocused and inconsistent in its application and should be reconsidered.

ix) Conflicts of Interest

Provisions 3.23 to 3.25

- 3.8 We assume that the above Provisions relate only to remuneration arrangements by which remuneration or benefits are paid or provided by a regulated entity to a sales employee or intermediary, in relation to the provision, arrangement or recommendation of a financial product or service to a consumer. We would therefore suggest that references to 'remuneration arrangements' in Provisions 3.23 and 3.25 be amended to refer to 'sales remuneration arrangements' to clarify the scope of these Provisions, and that the reference to 'including' is deleted from Provision 3.23.
- 3.9 Provision 3.23 states that "A *regulated entity* must not knowingly create situations that may give rise to a conflict of interest whose existence may damage the interests of a *consumer*..." We consider the word "may" is too vague in this context and as such it may be difficult to comply with the Provision.
- 3.10 Similarly the word "potential" in Provision 3.25 creates an ambiguous and indefinite requirement.
- 3.11 We assume that Provisions 3.23 and 3.25 are not intended to ban the payment of commissions or other forms of sales remuneration by a regulated entity. We therefore suggest that Provisions 3.23 and 3.25 should clarify that the act of a regulated entity paying sales remuneration, e.g. commissions, to an employee or intermediary is not itself a conflict of interest or acting against the consumer's best interests, in the absence of any other indication to the contrary. This is particularly relevant where a regulated entity may distribute the same or similar products and services through different distribution channels, as well as directly to consumers, at different prices.

- 3.12 We suggest clarification is needed that Provision 3.23 does not impinge on a regulated entity's freedom to offer a choice of sales remuneration scales to independent intermediaries. This choice enables the intermediary to choose from a menu of sales remuneration options (e.g. front-end versus spread commission) when selling or providing a particular product or service to a consumer which may give rise to a different pattern of charges or benefits for the consumer.
- 3.13 By referring to 'letter of appointment', Provision 3.24 implicitly refers only to Investment Intermediaries Act authorised intermediaries. 'Letter of appointment' is a requirement of the Investment Intermediaries Act 1995 but is not a requirement of registration as an insurance intermediary under the European Communities (Insurance Mediation) Regulations 2005. Provision 3.24 therefore does not apply to intermediaries who are only registered insurance intermediaries, nor to individual tied insurance agents for whose actions an insurer has taken full and unconditional responsibility. As currently drafted, it creates a potential distortion in the marketplace by applying to some but not all distribution channels.

4 Queries

We would be delighted to assist if clarification or elaboration is required on any of the points made in this submission. Please direct any queries to Ms Yvonne Lynch, Director of Professional Affairs, at the contact details at the end of this submission.

Appendix A

**Extract from Response to the Central Bank of Ireland’s Consultation Paper 47
(CP47), “Review of the Consumer Protection Code”.**

Response to questions 11 to 14

Product Producer Responsibilities

11. In relation to identifying a target market of consumers for a product, what are the key consumer criteria that you believe should be used?

Under Chapter 3, Provision 43 of the proposed Code, when designing an investment product, a product producer must “identify the target market” for the product. The target market “must only comprise the types of *consumer* for which the product is likely to be suitable”. The product producer must also identify “the target market for which the product is not suitable”.

Presumably “identifying a target market” in question 11 means identifying the types of consumer for which a product might or might not be suitable (rather than making a business decision to target a particular market)³.

We suggest that the key consumer criteria used to identify types of consumer for which a product might or might not be suitable should include:

- Investment objectives
 - o Which consumers will this product suit / not suit – those who require security of capital? or capital growth? or a steady income? or a guaranteed return? or exposure to a particular asset class? etc.
- Investment time horizon and need for liquidity
 - o Is the product designed for persons who want (and, for medium- to long-term investments, have the capacity) to invest on a short-, medium- or long-term basis?
 - o To what extent do features such as restrictions on access to the investment, or charges for early exit, or investment in assets that may be vulnerable to prolonged periods of price volatility, impact on the suitability or otherwise of the product for various types of consumers?
- Attitude to risk
 - o Which consumers will this product suit – e.g. those who need modest returns and low risk, or those who are seeking higher returns and higher risk, etc?
 - o Capacity to withstand adverse outcomes: is the level of investment risk such that the product would not be suited to certain types of consumers, or would be suitable only for a limited proportion of an investment portfolio?
- Level of investment knowledge / experience

³ We believe that products should be designed to meet identified consumer needs. It follows from this that the consumers for whom a product is suitable should be identified before the product is designed, rather than *vice versa*. The key investment criteria listed in the response to question 11 can be used to articulate the types of consumer for which a product is or is not suitable. They can also be used to segment a customer database in order to identify potential target markets or design marketing programmes. However, when deciding which of the potential markets it will target, a product producer will also consider questions such as the size of the markets, product profitability and advisers’ availability to sell the appropriate products to the chosen market.

- How complex is the product? Does it include features such as gearing or investment in exotic assets? To what extent would investment knowledge / experience be required in order to understand the product fully? How does this impact on its suitability or otherwise for various types of consumers?

To “identify” a target market may be interpreted as to “ascertain” the target market, and it is not clear from the proposed Code that there will be any obligation on product producers to communicate the target market to consumers or intermediaries. We recommend that the proposed Code be amended to explicitly require regulated entities to state the types of consumer for which a product is likely to be suitable, and the types for which it is not suitable, in the brochure or other materials normally used to market the product to consumers.

We suggest that consideration be given to requiring product producers to list, in their marketing materials and on a product-specific basis, types of consumer who might be vulnerable consumers in respect of (and having regard to the characteristics of) each product. Using this as the reference point may be more effective than requiring that suitability be assessed by reference to a very broad definition of vulnerable consumer, as proposed under Chapter 5, paragraph 10.

12. Is the consumer information listed in Chapter 4, Provision 32 useful when identifying a target market?

As in question 11, presumably “identifying a target market” means identifying the types of consumer for which a product might or might not be suitable. The information in Chapter 4, Provision 32 is useful in considering scenarios to determine whether a product is suitable for a particular target market.

13. Do you agree with the requirements outlined in Chapter 3, Provision 45? How often do you think that reviews of products should be undertaken?

Under Chapter 3, Provision 45, if a product producer establishes that a product no longer meets the general needs of the target market for which it was designed, the producer must:

- (a) reassess the product to identify the consumer type for which it is suitable, and
- (b) immediately update the information it provides to intermediaries in relation to the product.

We agree with requirements (a) and (b), though options to modify or withdraw the product should also be included.

Requirement (c), to notify the Central Bank, requires further elaboration. What is to be notified? What details are required? How soon is notification required? What will the outcome of such notification be - what action will the Central Bank take (if any)?

We suggest that the wording of the Provision be amended to address the situation where it transpires that a product is taken up by a significant number of consumers beyond the target market for which it was designed.

We agree that an annual review of products should normally be sufficient. However, we believe that each product should have specified triggers (defined by the product producer) that require an immediate review. For example, for tracker bonds, a downgrade of a counterparty should automatically trigger a review.

14. Should product producers be required to periodically review applications for their investment products, received through their direct sales force and through the intermediary channel, to ensure that actual sales are consistent with the targeted market? Do you foresee any hurdles to the implementation of this requirement in practice?

We believe that this is a good idea and we understand that many product providers carry out this activity already. This activity should not be carried out in isolation but should be combined with other measures, such as monitoring of complaints, lapses, etc. In addition, rather than a prescribed format that might inadvertently foster a “tick box” approach, any review should be customised so as to focus on any risks inherent in the product, as identified during the product development process.



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