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EMEA Centre for Regulatory Strategy

European Commission proposals on a Revision of the Insurance Mediation Directive (IMD II) and Packaged Retail Investment Products (PRIPs)
Key changes and impact on firms

The proposals published by the European Commission on 3 July 2012 introduce rules aimed at levelling the playing field for the sale and disclosure of insurance and retail investment products, so as to strengthen consumer protection. PRIPs addresses disclosure rules for retail investment products and IMD II addresses sales and disclosure rules for insurance products, including additional sales rules for insurance investment products – insurance 'PRIPs'.

Both proposals have been some time in coming, following consultations in Autumn 2010. They pose significant strategic and operational challenges to providers and distributors in the insurance and retail investment markets. As anticipated, IMD II proposes to widen the scope of the Directive to include direct sales by insurance and reinsurance undertakings. It introduces strengthened conduct of business rules, particularly for insurance investment products, and increased professionalism requirements. It also contains surprises, explicitly bringing certain activities of insurance aggregator websites, claims managers and loss adjustors within scope of the Directive, and goes further than expected in some areas, notably in relation to remuneration disclosure and rules on cross-selling. PRIPs proposes the introduction of the Key Information Document (KID) when investment products are sold to retail consumers, but also steps away from the Consultation by not excluding certain pensions products and variable annuities from scope. Competent Authorities will also be given product intervention powers when KIDs fail to comply with the Regulation, or are not provided at all.

The principle behind the KID is generally seen as sound: consumers should have access to information that is easy to understand and facilitates straightforward comparison between investment products. If it achieves its aim, the KID has the potential to improve fundamentally consumers' engagement with investment products. However, considering the wide range of investment products that will be covered, it will be a challenge for firms and regulators to ensure that KIDs are of practical use to consumers and serve the purpose for which they are intended. By bringing certain activities within scope of the Directive and increasing transparency and conduct of business requirements, IMD II is likely to impact firms' business model decisions. While IMD II remuneration disclosure requirements aim to address potential conflicts of interest, remuneration structures differ across sales channels. Ensuring that consumers understand the context in which disclosures are made, and can make use of this information, will be important to avoid undermining the Commission's objective of a level playing field.

IMD II is intended to address gaps and inconsistencies in insurance mediation identified by the Commission during a 2005-2008 implementation check, following the IMD's initial adoption in December 2002. The PRIPs initiative, which has its roots in a 2007 Call for Evidence by the Commission on substitute investment products, aims to improve cross-sector transparency in the retail investment market. The initiative is no longer called PRIPs, but a Regulation on Key Information Documents for Investment Products. However, for the purposes of continuity in this briefing, we will continue to refer to the proposal as 'PRIPs'.

IMD II and PRIPs have been launched as a package by the Commission, alongside a further revision of the UCITS Directive (UCITS V). UCITS V similarly aims to promote consumer protection through introducing new provisions relating to UCITS depositaries, as well as new remuneration rules for UCITS managers (see UCITS V briefing for further details).

IMD II and PRIPs, while separate proposals, are linked. While disclosure requirements for investment products (including insurance investment products) will be addressed through PRIPs, sales rules will be addressed through IMD II and the Revision of the Markets in Financial Instruments Directive (MIFID II). MIFID II sales rules for non-insurance investment products will provide the blueprint for IMD II sales rules for insurance investment products. MIFID II proposals were published in October last year and are currently being negotiated. Splitting sales rules for investment products between two different Directives introduces the potential risk of discrepancies arising between the rules for insurance and non-insurance investment products during negotiations and when further measures and guidance are published. Any discrepancies would undermine the consistent and harmonised approach to the selling of investment products that the PRIPs initiative is seeking to achieve. The table below illustrates the application of sales and disclosure rules across IMD II, PRIPs and MIFID II.

	IMD II	**PRIPs**	**MIFID II**
Insurance (non-investment)	Sales and disclosure	n/a	n/a
Investment products (non-insurance)	n/a	KID disclosure	Sales and disclosure
Insurance investment products	Enhanced sales rules (MIFID II used as blueprint)	KID disclosure	n/a

This briefing provides an overview of the proposals followed by a more detailed look at the key changes contained in the proposals and the challenges they might bring for firms.

Overview of proposals	
IMD II	**PRIPs**
Objectives:	
Ensure a level playing field between all participants involved in selling insurance products to achieve improved consumer protection, greater market integration and undistorted competition.	Harmonise selling and disclosure rules for retail investment products across sectors in order to promote investor protection.
Who is affected?	
Insurance and reinsurance undertakings and intermediaries (includes certain activities of aggregator websites and insurance policies sold ancillary to the sale of services). Professional claims managers and loss adjustors are also now in scope.	Investment product 'manufacturers' and those who sell investment products to retail investors.

<table>
<tr><td colspan="2">Key changes:</td></tr>
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Expands the scope of the Directive to include sales by insurance and reinsurance undertakings (i.e. direct writers), certain activities of insurance aggregator websites (i.e. price comparison websites) and professional claims management and loss adjusting
Strengthened conduct of business and professionalism requirements, in particular relating to remuneration and cross-selling disclosure
Enhanced sales requirements for insurance investment products (in line with MIFID II)
Rules aimed at promoting proportionality and cross-border activity
Strengthened rules relating to complaints, redress and sanctions

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Definition of an ‘investment product’ to include investment funds, retail structured products and investments packaged as insurance policies. This includes certain pension products
Disclosure of the KID, a concise and highly standardised document, when selling investment products to retail investors
Investment product ‘manufacturer’ is responsible for preparing and maintaining the KID and held liable if the KID is misleading, inaccurate, incomplete or inconsistent with other information documents required by law
Strengthened rules relating to complaints, redress and sanctions. Competent authorities will be given product intervention powers when KIDs fail to comply with the Regulation, or are not provided at all

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<tr><td colspan="2">Key impact on firms:</td></tr>
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A need to assess business strategies for those activities brought into scope of the Directive and as a result of increased transparency requirements relating to remuneration and cross-selling
Read-across of MIFID II sales rules to insurance investment products, although anticipated, represent a large shake-up in insurance investment selling practices. The impact will vary across Member States depending on the extent that national regulators already include certain enhanced requirements for insurance investment products, as in the UK
Increased training requirements for staff, particularly in light of increased professionalism requirements (including a requirement for Continuing Professional Development)

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Strategic challenges resulting from the introduction of the KID include: increased competition across investment products; assessing product range; and undertaking a ‘gap analysis’ of implementation requirements
Operational challenges include: getting the KID content right; ensuring effective processes in KID production and maintenance; dissemination to distributors; and providing appropriate training

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<tr><td colspan="2">Regulation or Directive?</td></tr>
<tr><td>Directive (minimum harmonisation) - Member States will be able to go further in their rules for the purposes of consumer protection.</td><td>Regulation - removes scope for Member States to tailor requirements when they are transposed into national law meaning a more standardised approach to retail investment product disclosure across the EU.</td></tr>
<tr><td colspan="2">Implementation timeline:</td></tr>
<tr><td>If legislative negotiations are concluded within 2013, the Directive could be applicable in 2015.</td><td>If legislative negotiations are concluded within 2013, the Regulation could be applicable in 2015.</td></tr>
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IMD II

Key changes

We have identified six key changes in the Revision of the IMD proposal: 1) scope and definitions; 2) proportionality and cross-border entry to insurance markets across the EU; 3) professionalism; 4) information and conduct of business rules; 5) sales rules for insurance investment products; and 6) complaints, redress and sanctions.

1. Scope and definitions

In line with what was set out in the Consultation, the proposal confirms the Commission’s intention to widen the scope of the Directive to capture sales by insurance and reinsurance undertakings without the intervention of an intermediary i.e. direct writers. This aims to address inconsistencies in the sale of insurance and its impact is likely to vary across Member States depending on the extent to which competent authorities have already attempted to level the playing field through national rules. The definition of 'insurance mediation' has changed. In addition to including direct sales by insurance undertakings, it also now specifically includes certain activities of insurance aggregator websites (i.e. price comparison sites) and professional claims management and loss adjusting. Significantly, the term 'introducing', which had been interpreted differently across Member States, is removed from the definition. The definition of 'reinsurance mediation' is similarly amended. The definition of an 'insurance investment product' is introduced as a contract of insurance which is also an 'investment product' as defined in the PRIPs Regulation (see below). This is intended to allow the read-across of MIFID II sales rules to these products.

2. Proportionality and cross-border entry to insurance markets across the EU

With the aim of promoting proportionality for certain activities, the proposal introduces an exemption from registration with competent authorities for those who conduct insurance mediation on an ancillary basis (and who meet certain other conditions) and for professional claims managers and loss adjustors. They will instead only need to submit a declaration to the competent authority stating their identity, address and professional activities and will be subject to a 'light touch regime'; the full conduct of business and information requirements will not apply.

The Commission has also introduced rules aimed at improving cross-border entry to insurance markets across the EU, including enhancing transparency through requiring publication of general good rules applicable in Member States.

3. Professionalism

The proposal introduces increased professionalism requirements, such as a requirement for continuing professional development (CPD), whilst attempting to retain proportionality as those performing intermediary activities should 'complete their tasks and perform their duties adequately, demonstrating appropriate professional experience relevant to the complexity of the products they are mediating'.

The requirement to possess appropriate 'knowledge and ability', as determined by the Home Member State, is maintained, however, the Commission is empowered to adopt delegated acts to specify: the notion of what adequate 'knowledge and ability' means; criteria for determining appropriate professional qualifications, experiences and skills; and the appropriate CPD necessary to maintain an adequate level of performance. We will have to wait and see as to how onerous these requirements may be on firms. To promote cross-border trade, the proposal also sets out circumstances for the mutual recognition of such 'knowledge and ability' across Member States.

4. Information and conduct of business rules

The proposal imposes similar disclosure requirements on insurance undertakings as exist for insurance intermediaries and increases requirements in several significant ways, particularly with regard to remuneration disclosure and cross-selling. Certain exemptions exist for the mediation of 'large risks', mediation by reinsurance intermediaries or undertakings and in relation to professional customers, as defined in the annex to the proposal.

The Commission has stopped short of requiring MIFID conflicts of interest requirements (i.e. the requirement to identify conflicts and disclose them to the consumer where they cannot be managed), as they have required for insurance investment products (see below). Instead, they have sought to address conflicts of interest through increased remuneration transparency.

Insurance intermediaries and undertakings will be required to disclose the nature and the basis of the calculation of any variable remuneration (i.e. sales bonus) received by employees during distribution of the insurance product. In addition, the basis (i.e. fee and/or commission) and amount of fee or commission should be disclosed by insurance intermediaries. If the amount of the commission is based on the achievement of agreed targets or thresholds, the targets or thresholds as well as any amounts payable on achieving them, should also be disclosed. With the aim of allowing a longer lead-in time for non-life intermediaries, the disclosure requirements relating to the amount of fee or commission received for the intermediation of non-life products will be ‘on request’ for the first five years following the Directive coming into force, before full disclosure is required. The Commission will set out further detail on this regime in delegated acts.

In line with MIFID II proposed rules on cross-selling, the proposal sets out that when an insurance product or service is offered together with another product or service as a package, the customer should be told: that the components of the package can be bought separately; and information on costs and charges of each component of the package that can be bought separately. ‘Bundling’ practices can continue, subject to the above, however, ‘tying’ will no longer be allowed i.e. defined as ‘offering one or more ancillary services with an insurance service or product in a package where this insurance service or product is not made available to the consumer separately’.

A requirement is introduced that the insurance intermediary or undertakings, when carrying out mediation activities, should act ‘honestly, fairly and professionally in accordance with the best interests of its customers’ and all information disclosed to consumers should be ‘fair, clear and not misleading’. Prior to the conclusion of a contract, IMD II also proposes a requirement that the consumer should be given sufficient information about the product to allow an informed decision on its purchase to be made.

5. Sales rules for insurance investment products: additional customer protection requirements

The proposal introduces a new chapter specifying additional requirements that relate to the sale of insurance investment products by insurance undertakings or intermediaries. As expected, these read-across MIFID II conflicts of interest and investor protection provisions, with the aim of harmonising selling practices across all investment products. The requirements include:

- Conflicts of interest must be identified and disclosed to the customer where they cannot be managed appropriately;
- In line with above, a requirement to act ‘honestly, fairly and professionally in accordance with the best interests of customers’ and ensure that information is ‘fair, clear and not misleading’;
- Appropriate information should be provided to customers and potential customers about the services they will receive, in particular regarding advice and costs and associated charges.
- Advice may be classed as independent under certain conditions which include: assessing a ‘sufficiently large number’ of products; not being limited to products where close links exist with the insurance intermediary or insurance undertaking; and not accepting or receiving fees, commissions or any monetary benefits paid or provided by any third party;
- Information must be obtained from a customer in order to assess suitability, for advised sales, and appropriateness, for non-advised sales, with different requirements for each; and,
- A requirement for periodic and adequate reports to customers on the service provided.

Importantly, the proposal does not read-across the MIFID II exceptions to the appropriateness test for non-advised sales, where appropriateness does not need to be assessed when certain conditions are met, for example if the sale is in relation to a non-complex product. This would therefore suggest that the Commission has concluded that all insurance investment products are complex and require an appropriateness assessment. While many insurance investment products are undoubtedly complex, there are many different types of products on the market which range in complexity and the Commission has not provided flexibility in this rule.

6. Complaints, redress and sanctions

The proposal introduces tougher rules relating to sanctions. Sanctions or measures imposed for breaches must be published by both competent authorities and, on an annual basis, by the European Insurance and Occupational Pensions Authority (EIOPA). The rules also require effective mechanisms to encourage the reporting of breaches, including protections for ‘whistle-blowers’ and their personal data.

Member states are now required, rather than encouraged, to set up appropriate, effective, impartial and independent complaints and redress procedures for the out-of-court settlement of disputes. However, this is unlikely to be of significant impact as the majority of Member States already have an existing dispute resolution body that covers insurance, such as the Financial Ombudsman Service in the UK.

IMD II - key challenges for firms

As identified by the Commission, the minimum harmonisation nature of the IMD has led to a ‘patchwork’ of national regulations related to insurance sales across Member States. Therefore, the impact of IMD II may vary across Member States depending on existing national regulations. For instance, the UK and Italian regulators have already read across certain aspects of MIFID to insurance investment products, in the case of the UK, and to certain categories of life insurance products, in the case of Italy. Finland has relatively strict rules relating to insurance sales and has gone further than other Member States by banning brokers from receiving commission. In Belgium, the conduct of business regulator, FSMA, is consulting on setting out “MIFID-like” rules to “independent financial planners” in relation to their “asset advice” including advice on certain types of insurance and pension products. Nevertheless, the proposals will have a significant impact on firms whose activities have been brought into scope or where increased requirements represent a shift from current practices.

A need to assess business models?

- Activities in scope

Insurance undertakings, particularly where the majority of their sales are conducted through intermediaries, may see an advantage in concentrating on intermediated sales to avoid complying with the Directive. Likewise, the removal of the term ‘introducing’ from the definition of insurance intermediation may prove important for business strategy. Depending on final transposition of the Directive into national rules, certain firms, particularly those which sell insurance ancillary to the provision of other services, may see an advantage in ‘introducing’ consumers to intermediaries, rather than comply with relevant requirements under IMD II. Aggregator websites will need to assess the impact of the conduct of business requirements, in particular conflicts of interest disclosures, on their business models. They will need to ensure that they have appropriate controls, processes and due diligence in place.

- Remuneration transparency

The significance that consumers will place on the remuneration costs associated with a product, when compared to the total cost of the product, and how this might impact buying decisions, is unclear. The Commission’s aim in increasing remuneration transparency is to ensure that the consumer is more aware of potential conflicts of interest. In this regard, it is likely that the increased transparency will put pressure on sales remuneration, fees and commission. Remuneration structures across sales channels differ and it is likely that direct writers will be at an advantage to intermediaries as they may find it more straightforward to internalise distribution costs.

Firms are likely to consider forms of remuneration that may lessen the impact of the rules. For instance, there may be a trend towards more fixed rather than variable remuneration i.e. salaries as opposed to bonuses, although there will need to be a balance struck between keeping disclosed costs low and incentivising employees and distributors. Calculating the fees or commission which should be disclosed will be less than straightforward for intermediaries. We will have to wait for Level 2 for further clarity on this rule.

- Cross-selling

There is also likely to be pressure on costs and charges relating to components sold in a ‘package’. As these become more transparent to the consumer, they are more likely to assess the value they place on each additional component and may conclude that they do not require additional components or decide to buy these elsewhere. In particular, this may be felt hardest in highly competitive markets where margins are already squeezed and where firms have pursued cross-selling as a strategy to boost revenue. These disclosures may mean firms having to re-think these strategies.

This focus by the Commission on insurance product cross-selling and transparency could also indicate the direction to come with regards to other non-MIFID products such as bank accounts, where the Commission identified issues of transparency and comparability in bank account fees in its March 2012 Consultation.

Additional requirements for retail investment products

The proposed changes with regard to insurance investment products aim to harmonise requirements across investment products and, as such, have been widely anticipated. Nevertheless, they represent a large shake-up in insurance investment selling practices, the impact of which will vary across Member States depending on the extent to which national regulators have already gone further than the IMD in their rules. Firms which are already subject to current MIFID sales rules in parts of their business, such as larger banks, may find the new rules less challenging to implement than, for example, smaller insurance intermediaries. They may also find that there are benefits arising from a more harmonised selling regime, allowing streamlining of training and practices and increased centralisation of functions, for example compliance functions.

In the UK, the proposals regarding advice follow a similar direction to requirements under the Retail Distribution Review, which will come into effect at the end of this year. However, any differences in requirements, for instance as regards the definition of independent advice or products caught, may pose challenges firstly to the Financial Services Authority and then to firms.

Requiring the appropriateness test for all insurance investment products places a greater regulatory burden on the sale of insurance investment products as compared to non-complex investment products. This may put insurance investment product sales at a disadvantage. As the MIFID II and IMD II rules are negotiated, any inconsistencies in investment selling practices that emerge between the two Directives are also likely to pose additional challenges.

Operational requirements and training

In addition to strategic challenges, firms will face operational challenges in complying with the proposed rules. In particular, employees will need to be trained on the new rules and face increased professionalism requirements, including CPD.

PRIPs

Key changes

We have identified five key changes in the PRIPs proposal: 1) scope; 2) form and content of KIDs; 3) responsibility and liability; 4) interaction with other disclosure requirements; and 5) complaints, redress and sanctions.

1. Scope

The Regulation will apply to all ‘investment product manufacturers’ regardless of sector, for example, fund managers, insurance undertakings, issuers of securities, credit institutions or investment firms. A ‘manufacturer’ includes those who makes changes to an existing investment product by altering its risk and reward profile or associated costs. The Regulation will also apply to anyone who sells an investment product to a retail investor. This will be the distributor or the ‘manufacturer’ in the case of a direct sale.

The Regulation covers ‘investment products’- the ‘P’ and ‘R’ have been dropped from ‘PRIPs’ but the Commission’s intention appears to remain the same. Investment products are defined as where ‘the amount repayable to the investor is exposed to fluctuations in reference values or in the performance of one or more assets which are not directly purchased by the investor’. This still captures the concept that the investor, while exposed to asset fluctuations, does not have a direct holding and so a form of ‘packaging’ or ‘manufacturing’ exists. The ‘retail’ element is still present as it is relevant at the point of sale. Products such as investment funds, retail structured products and investments packaged as insurance policies will be caught in the ‘investment product’ definition. The proposal lists products which will be specifically excluded from scope, such as insurance products that do not offer investment opportunities, products exposed solely to interest rates, and direct investments, for example, in corporate shares or sovereign bonds.

Importantly, and in contrast to the Consultation, investment products ‘used as individual retail pension products, i.e. accumulation vehicles for the purposes of retirement planning’ are in scope. The term ‘pension products’ is defined. Occupational pension schemes which fall under the scope of the Solvency II Directive or the Institutions for Occupational Retirement Provision (IORP) Directive and pension products ‘for which a financial contribution from the employer is required by national law and where the employee has no choice as to the pension product provider’ are specifically ruled out of scope. Due to the particularly heterogeneous nature of the pensions landscape across Member States, the complexity of harmonising rules relating to pensions could also risk delays to the initiative as a whole. ‘PRIPs inspired’ rules for occupational pensions will be something to watch out for as the Commission reviews the IORP Directive.

2. Form and content of Key Information Documents (KIDs)

The Commission intends to meet its aim of harmonised disclosure requirements across retail investment products through the introduction of KIDs when investment products are sold to retail clients. KIDs will have a strongly standardised “look and feel” to facilitate easy comparison and comprehension by retail investors. They should be ‘accurate, fair, clear and not misleading’, short and concise and written in non-technical, jargon-free language. Lessons learned from UCITS KIID implementation suggest that this will be easier said than done.

The proposal sets out specific information to be included in the KID. While KIDs, as proposed, follow the ‘principles’ of the UCITS Key Investor Information Documents (KIID), which became mandatory for sales of all UCITS from 1 July this year, they differ in certain respects. For example, they introduce additional sections such as an indication of whether loss of capital is possible and the recommended minimum holding period and expected liquidity profile of the product. There are also additional disclosure requirements where specific environmental, social or governance outcomes are targeted by the manufacturer and for pension products regarding projections of possible future outcomes. A ‘common symbol’ should be displayed on the KID to distinguish it from other documents. Further detail is expected at Level 2, particularly regarding the all important methodology underpinning the presentation of risk and reward and the calculation of costs.

It is not yet clear at this stage what would be required in the case of the insurance investment product, for example an investment bond in the UK, where a consumer may be offered a wide range of possible funds choices within a single product. A balance will need to be struck between ensuring that the KID contains sufficient information so that it is useful to the consumer in the decision-making process, whilst not overburdening them with too much information.

3. Responsibility and liability

PRIPs proposes to make the investment product manufacturer responsible for preparing and maintaining the KID. Similar to UCITS KIID requirements, the person selling the product to a retail investor is required to provide the KID, free of charge, in good time before the sale (with certain exceptions). The proposal also sets out the medium in which the KID should be disclosed.

In addition to the initial preparation of the KID, manufacturers will also need to review their KIDs regularly and ensure they are kept up to date. Further detail on the relevant conditions for maintaining the KID is to follow at Level 2, including the circumstances in which retail investors should be informed about a revised KID for an investment product they have purchased. Effective processes will be necessary to ensure that updating and distributing new KIDs does not become a ‘never-ending’ process.

The manufacturer will be held liable if the KID is misleading, inaccurate or incomplete, or it contains information that is inconsistent with other information documents required by law. Delegation to a third party will not change this overall responsibility and so this risk will need to be managed when considering outsourcing. The ‘burden of proof’ will fall on the manufacturer, rather than on the consumer, to prove that the KID was drawn up in compliance with the Regulation.

4. Interaction with other disclosure requirements

The KID is expected to be a stand-alone document, clearly separate from marketing materials. As the Commission intends it to serve a specific purpose different to other disclosure requirements, such as under Solvency II or the Prospectus Directive, it will exist in parallel to these Directives. However, the Commission has indicated that it is open to addressing the case for removing duplication across disclosure requirements in future. In the meantime, manufacturers will not be able to produce the KIDs in isolation but will need to review all disclosures for each investment product, whether marketing materials or those required by law, to ensure consistency.

While UCITS fall under the ‘investment product’ definition, the Commission proposes a five year transitional period before determining whether: they should be subject to the PRIPs Regulation (with the relevant KIID provisions repealed from the UCITS Directive); the relevant rules in the separate Directives should be maintained, but aligned; or the transitional period should be extended. This will follow a review of the effectiveness of the PRIPs Regulation which is set to take place four years after its implementation.

5. Complaints, redress and sanctions

New to the initiative, competent authorities will be given product intervention powers when KIDs fail to comply with the Regulation, or are not provided at all. Sanctioning powers include: prohibiting or suspending marketing of retail investment products; requesting production of a new KID; and/or informing retail investors of their rights and where they can direct complaints or claims for redress. There will be increased disclosure to the public where firms fail to comply. Firms will need to ensure they give the KID requirements appropriate attention to ensure compliance and to avoid the risk of delays to product marketing or being identified in public disclosures.

In terms of complaints, the Regulation sets out that investment product manufacturers must establish appropriate complaints procedures and, as also proposed in IMD II, Member States must establish procedures for the out-of-court settlement of disputes.

PRIPs - key challenges for firms

The Regulation will affect firms, both at a strategic and operational level.

1. Strategic challenges

Competition - the aim of the KID is to increase transparency for retail investors, allowing them to directly compare like-for-like products as well as different products that may also meet their needs. Investors will be able to compare, for example, insurance investment products with other investment funds across similar categories as set out in the KID. This is likely to drive competition across retail investment products. Investors and distributors are likely to favour well-written KIDs – it will be important to get this right.

Rationalise product range - manufacturers which find they have multiple products with similar characteristics may want to rationalise their product range so that retail investors are offered a meaningful choice of products. This would also reduce the challenge of producing and maintaining multiple KIDs which have similar offerings.

Gap analysis - the manufacturer will need to take stock of existing products and determine which products are in scope of the Regulation. They will need to assess IT requirements, people aspects including capacity and existing and required processes. Where a gap is identified, the manufacturer will need to determine whether to fill the gap themselves or whether to outsource, whilst taking into account that liability for the KID will remain with the manufacturer.

2. Operational challenges

Content of KIDs - manufacturers will need the right information and present it in the right way, ensuring language is simple, consistent with other materials and translated appropriately. Lessons learnt from implementing UCITS KIIDs suggest frequent content issues that arise are: the difficulty of expressing complex terms in plain language whilst remaining consistent with other materials; and the use of excessive information or generic wording. Unstructured text and weak translations are also common problems.

Data quality and integrity will also be important in calculating risk, charges and performance. Learning from the UCITS KIID example, the risk indicator will depend on product classification and will need to be monitored on an ongoing basis. The definition and isolation of elements that will need to be included in the charge figure may become a cumbersome process and drive review of charge structures if it appears that costs compare unfavourably with competitors or other investment products.

Producing and maintaining KIDs - a key impact on product manufacturers is likely to be the sheer number of KIDs that will need to be produced from scratch. Manufacturers will need to take stock of all their investment products and are likely to need a production process on an industrial scale. A key issue identified in the UCITS KIID implementation process has been ensuring that all teams are working off the same lists to avoid unnecessary clarification and reconciliation discussions.

In addition to producing the KID, manufacturers will also need a process in place to ensure that their KIDs are kept up to date (and reviewed at least annually), identifying when an update is needed and then implementing the update.

Dissemination of KID to distributors - a process will need to be established whereby distributors can access up-to-date KIDs in good time.

Training - manufacturers will need to train staff in KID production and process and distributors will require training on how to review KIDs.

The bigger picture

In response to the financial crisis and following several recent mis-selling scandals and a recognition that products are becoming more complex, there has been increased focus on consumer protection in financial services by both regulators and policymakers. We have seen a raft of recent initiatives which seek to achieve this aim in a number of ways, for example, through focusing on the point of sale, using improved disclosure or other conduct of business requirements, or by intervening in the product itself.

At the international level, the October 2011 *G20 High-Level Principles on Financial Consumer Protection,* developed by an OECD Task Force, set out common principles that countries should adopt in order to strengthen consumer protection. IOSCO's February 2012 *Consultation on Suitability requirements for Complex Financial Products* recommends common principles in the face of increasing complexity in financial products.

In the EU, the proposals follow other initiatives which seek to advance the consumer protection agenda. Notably, the recent MIFID II proposals aim to promote greater independence in services for consumers through introducing structural changes to the remuneration of portfolio managers and independent investment advisers, while the Markets in Financial Instruments Regulation (MIFIR) introduces 'product banning' powers for national regulators and ESMA. As noted earlier in the briefing, the PRIPs KID follows the introduction of the UCITS KIID, which became mandatory for sales of all UCITS by 1 July this year.

Deloitte's September 2011 **Product Intervention briefing** provides an overview of some recent national initiatives regarding product intervention. Deloitte's April 2012 **Product Governance** report analyses the effect of product governance regulatory initiatives on the UK market and the rest of Europe. In terms of disclosure, some national initiatives take the UCITS KIID further. For example, the Netherlands, Germany and France have already extended UCITS KIID requirements to non-UCITS. Outside the EU, Switzerland imposes KIIDs on foreign UCITS and non-UCITS, with Swiss specific information to be added, and Norway accepts KIIDs.

We can only expect policymakers' and regulators' focus on consumer protection to continue. However, considering the multiple ways in which this can be achieved and the multiple regulations which apply across products, a form of harmonisation and consistency will be important to ensure changes meet their objectives while avoiding undue burden on firms.

What's next?

The proposals will pass to the European Parliament and to the Council for negotiation and adoption. Assuming both sets of negotiations are concluded within 2013, which may be an ambitious timetable, IMD II and PRIPs could be applicable from 2015.

While this may still seem a long way off, there are things which firms can and should be doing now in preparation for these changes. As we wait for some of the details to be filled in, firms can begin addressing the strategic aspects of the proposals and assessing their capabilities, products and processes.

Regards

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