

Supervisory Statement

On assessment of value for money of unit-linked insurance products under product oversight and governance

EIOPA(2021)0045739
30 November 2021



eiopa

European Insurance and
Occupational Pensions Authority

1. LEGAL BASIS

- 1.1. The European Insurance and Occupational Pensions Authority (EIOPA) provides this Supervisory Statement on the basis of Article 29(2) of Regulation (EU) No 1094/2010¹. This Article mandates EIOPA to play an active role in building a common Union supervisory culture and consistent supervisory practices, as well as in ensuring uniform procedures and consistent approaches throughout the Union.
- 1.2. EIOPA delivers this Supervisory Statement on the basis of Article 25 of Directive (EU) 2016/97² (IDD) and Commission Delegated Regulation (EU) 2017/2358³ (POG Delegated Regulation), in particular Articles 4, 5, 6, 7 and 8 thereof.
- 1.3. This Supervisory Statement is addressed to the competent authorities⁴, as defined in Article 4(2) of Regulation (EU) No 1094/2010.
- 1.4. The Board of Supervisors has adopted this Supervisory Statement in accordance with Article 2(7) of its Rules of Procedure⁵.

¹ Regulation (EU) No 1094/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Insurance and Occupational Pensions Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/79/EC (OJ L 331, 15.12.2010, p. 48).

² Directive (EU) 2016/97 of the European Parliament and of the Council of 20 January 2016 on insurance distribution (OJ L 26, 2.2.2016, p. 19).

³ Commission Delegated Regulation (EU) 2017/2358 of 21 September 2017 supplementing Directive (EU) 2016/97 of the European Parliament and of the Council with regard to product oversight and governance requirements for insurance undertakings and insurance distributors (OJ L 341, 20.12.2017, p. 1).

⁴ Notwithstanding the fact that specific points of this Supervisory Statement describe supervisory expectations for insurance undertakings and insurance intermediaries, they are required to comply with the regulatory and supervisory framework applied by their competent authority based on Union or national law.

⁵ Decision adopting the Rules of Procedure of EIOPA's Board of Supervisors, available at: https://www.eiopa.europa.eu/sites/default/files/publications/administrative/bos-rules_of_procedure.pdf

2. CONTEXT AND OBJECTIVE

- 2.1. Since the first annual EIOPA Consumer Trends Report EIOPA has been highlighting concerns with regard to issues in the European unit-linked market including hybrid products that combine a unit-linked component with a profit participation component and/or a capital guarantee. Hereafter unit linked and hybrid products will be collectively referred to as ‘unit-linked products’.
- 2.2. As shown in the EIOPA Costs and Past Performance Reports costs can have a significant impact on returns of all insurance-based investment products. And while well-designed unit-linked products can provide significant benefit to consumers, allowing them to seek higher returns, unit-linked products which are not designed in a customer-centric manner continue to be a prominent area of concern,⁶ with competent authorities reporting a number of issues, such as: high complexity, mis-selling, mismatches between actual returns and customers’ expectations. Issues related to these products, in particular aspects relating to the poor value these products offer, dominate EIOPA’s conduct of business oversight platform work, EIOPA’s bilateral discussions with competent authorities, and EIOPA’s market monitoring activities – including those focused on COVID-19. EIOPA’s first comprehensive Thematic Review also focused on issues in this market.⁷
- 2.3. Because of the specific risks relating to (some) unit-linked products, some competent authorities have already started taking actions to address these risks. With a view of ensuring a common approach for addressing value for money risks – i.e. risks that products do not offer value to the target market to whom they are offered – EIOPA has developed a framework which was issued for public consultation between 13 April and 16 July 2021.
- 2.4. The analysis of the responses to the public consultation showed that it is widely understood that aspects related to value for money are already embedded in the IDD, albeit implicitly. In particular, Article 25 of the IDD and the POG Delegated Regulation require manufacturers to test whether products are aligned with the target market’s needs, objectives and characteristics. In fact, value for money aspects are included in what EIOPA already defined

⁶ See EIOPA 2021 Costs and Past Performance Report, at page 7 and 40. Available at [Cost and past performance report 2021.pdf - EN \(4\).pdf](#)

⁷ Available at https://register.eiopa.europa.eu/Publications/Reports/16.%20EIOPA-BoS-17-064-Report_Thematic%20review%20on%20monetary%20incentives%20and%20remuneration.pdf

as ‘fairness testing’ when outlining its approach to the supervision of product oversight and governance.⁸

- 2.5. However, because of the novelty and principles-based nature of these requirements, there are disparities in both how the manufacturers and distributors of unit-linked products implemented these requirements and how competent authorities measure and understand related risks and how they supervise these requirements.
- 2.6. It is therefore important to develop a common approach for addressing value for money risk. To this end, this Supervisory Statement sets out a framework which fosters that national supervisory approaches ensure that manufacturers’ and distributors’ implementation of product oversight and governance (POG) rules follow common principles when assessing the value for money risks in the unit-linked market as part of POG supervision. This supervisory statement is designed to assist competent authorities in supervising the manufacturers’ and distributors’ POG implementation.
- 2.7. It is important, however, to emphasise that POG supervisory activities do not aim at interfering with business decisions, rather they assess whether the process followed by manufacturers is sufficiently customer centric and considerate of the services and benefits offered in light of product features and the target market’s need, objectives and characteristics.
- 2.8. A risk-based approach to value for money risks is recommended, whereby those products which pose the greatest risk of consumer detriment due to poor value for money are given supervisory priority.

⁸ Available at [EIOPA’s approach to the supervision of product oversight and governance | Eiopa \(europa.eu\)](https://www.eiopa.europa.eu/en/opa/opa-approach-to-the-supervision-of-product-oversight-and-governance)

3. SUPERVISORY STATEMENT

HOW TO DEFINE VALUE FOR MONEY

- 3.1. The POG Delegated Regulation sets out that the product approval process has to ensure that products are aligned with the needs, objectives and characteristics of the target market and do not adversely affect customers, in order to prevent customer detriment. Considering that no target market has as its objective receiving poor value, it is clear that unit-linked products which offer poor value are not aligned with the objectives of any target market and should therefore not be marketed to consumers. Target markets differ substantially, hence product characteristics including features which may or may not offer value should be assessed vis-à-vis the target markets' needs objective and characteristics.
- 3.2. EIOPA considers that unit-linked products offer value for money when costs and charges are proportionate to the benefits (i.e. investment performance, guarantees, coverage and services) to the identified target market as well as reasonable, taking into account the expenses born by the providers.
- 3.3. As evidence of the assessment of value for money risks in their products, manufacturers should be able to present a structured **pricing process** as part of their POG documentation to provided competent authorities, which includes evidence that:
 - 3.3.1. costs and charges are properly identified, quantified and not undue;
 - 3.3.2. adequate and sufficient testing has taken place on whether the product offers value for money taking into account the needs, objectives and characteristics of the target market, through the lifetime of the product;
 - 3.3.3. costs and charges, investment performance, guarantees, coverage and services offered are regularly reviewed.
- 3.4. Moreover, manufacturers should also be able to present that they have developed their own notion of complexity and have placed their products on a complexity scale whereby the granularity of the target market is proportional to the product complexity. The more complex a product is, the more granular the target market should be. Higher complexity may result in more advice being required at the point of sale, leading to higher costs.

COSTS AND CHARGES NEED TO BE DUE

- 3.5. Due costs are costs charged to customers which are consistent with the target market's needs and objectives and are clearly identified and quantified. In particular, due costs are those costs which manufacturers can clearly link to services rendered or expenses made and which are proportional to the efforts and expenses incurred by the (co)-manufacturer or distributors. To this end, NCAs should monitor that the pricing **process** adopted by the manufacturer allows a clear identification and quantification of all costs charged to customers.
- 3.6. In addition, costs which are not specifically attributable at product level, such as overhead costs, brand marketing, cost of capital, etc., can also be considered due as long as the manufacturer clearly identifies and quantifies them in the pricing process and charges them to customers in reasonable proportion.
- 3.7. Costs in the unit-linked market often are charged to customers as a percentage of the premium paid, the unit value or a combination of these components. This means that the quantum of the charges is dependent on the size of the policy and the performance of the units. To be able to assess the level of charges for customers the structured pricing process could establish a range of premiums and performances on which the costs and charges are based.
- 3.8. For the identified costs, competent authorities should assess whether the insurance product manufacturer has sufficiently established that the costs are proportionate compared to market standards, to the type of service provided and to the target market's needs, objectives and characteristics. In particular, it is expected that underlying funds managed by affiliated entities are only made available when they offer at least similar value for money than comparable funds on the market. These assessments should be evident in the product design, product testing and pricing process and systems and controls should be in place to ensure conflicts of interest are managed and mitigated.

CLOSE LINK BETWEEN TARGET MARKET'S GRANULARITY AND PRODUCT COMPLEXITY

- 3.9. Unit-linked products require a high degree of financial literacy for customers to understand and make an informed decision on their purchase. More complex unit-linked products require a higher degree of understanding from insurance distributors. Manufacturers should be fully aware of this challenge and reflect this in their product design.
- 3.10. When defining the target markets for their unit-linked products, manufacturers should place these products on a complexity scale based on their own notion of complexity and ensure that the granularity of the target market clearly reflects the product's complexity.

- 3.11. A multitude of options in terms of underlying funds, levels of capital guarantees, and insurance features bring more choice for customers. This, however, increases the complexity of a product and thereby raises the level of advice required as well as the time and literacy required by the customer to make a well-informed decision. Therefore, it is important that differing options adequately reflect different needs, objectives and characteristics of customers belonging to the target market and that these aspects are also taken into account in defining a sufficiently adequate distribution strategy which aims at mitigating possible risks for customers.
- 3.12. The needs, objectives and characteristics of the target market should also reflect differences in terms of value offered by different options, as these may significantly differ and therefore need to have significantly different target markets.

ADEQUATE AND SUFFICIENT TESTING OF THE PRODUCTS' VALUE FOR MONEY

- 3.13. Manufacturers should test their unit-linked products appropriately, including via scenario analyses. This should be done before bringing to the market new products or products that have been significantly adapted, or when the needs, objectives and characteristics of the defined target market or the risks posed to it have significantly changed.
- 3.14. Such product testing, to be performed by manufacturers, should assess whether the unit-linked product over its lifetime meets the identified needs, objectives and characteristics of the target market. This includes delivering value for money, whereby value should be assessed taking into account the point in the lifecycle where target market could be reasonably expected to surrender the policy depending on its characteristics. For example, a product sold to target markets which may not have other non-financial and/or financial assets should deliver value prior to the recommended holding period, as the target market, because of its characteristics, could be considered to surrender earlier.
- 3.15. Manufacturers should always test unit-linked products in a qualitative and quantitative manner. Manufacturers should test the main features and characteristics of the insurance products and assess their value contribution to the needs and objectives of the identified target market.
- 3.16. The pricing process should evidence that each product feature delivers value for money in line with the needs, objectives and characteristics of the target market. This includes all underlying funds, levels of capital guarantees, available biometric risk covers, etc. For example, a product which offers high value because of the biometric risk cover while offering

average returns may bring value to target markets whose objectives is to accumulate capital whilst having adequate biometric coverage. However, such product would not offer value to target markets whose objective is to increase capital by seeking higher returns.

REGULAR REVIEW OF THE COSTS AND CHARGES, THE PERFORMANCE AND THE SERVICES OFFERED

- 3.17. Manufacturers should continuously monitor and regularly review unit-linked products they have placed on the market, to identify events that could materially affect the main features, the risk coverage or the guarantees of those products. They should assess whether the products remain consistent with the needs, objectives and characteristics of the identified target market and whether those products are distributed to the target market or is reaching customers outside the target market.
- 3.18. For unit-linked products it is of particular relevance to review the performance of the underlying funds. The underlying funds provide different options of the product (multi-option-products - MOPs) and as such the individual funds represent different product features. Manufacturers should define the notion of a product feature that is implemented by the individual underlying fund. The performance of the underlying funds should be reviewed with the regard to this defined notion of this product feature that is implemented by the specific underlying fund.
- 3.19. The performance after fund costs should be benchmarked against market returns. Actively managed funds should reflect the target market's needs, objectives and characteristics and manufacturers should evaluate whether their outperformance counterbalances the higher costs of active management.
- 3.20. Manufacturers that identify during the lifetime of a unit-linked product any circumstances related to the product that may adversely affect the customer of that product, should take appropriate action to mitigate the situation and prevent further occurrences of the detrimental event. This includes established underperformance of an underlying fund or the availability of funds with similar investment strategies but lower costs and hence better projected returns after costs.
- 3.21. Beyond regular reviews, reviews should also be triggered by ad hoc events which may adversely impact the products and/or the target market. This includes a sudden devaluation of the units which is not in line with the expected volatility for the relevant underlyings.

SUPERVISION OF THE POG PROCESS AS REGARDS TO VALUE FOR MONEY IN THE UNIT-LINKED MARKET

- 3.22. Competent authorities are expected to monitor their market to ascertain that insurance product manufacturers ensure that customers receive fair value unit-linked products. To this end competent authorities should monitor their markets and have internal metrics and benchmarks at their disposal to identify products which, based on their supervisory assessment, do not deliver value for money.
- 3.23. For such products, competent authorities should review the POG processes, including on value-for-money considerations, through a risk-based analysis during different supervisory activities as appropriate, which can include:
- a) off-site supervision;
 - b) on-site inspections;
 - c) thematic reviews.
- 3.24. Competent authorities should ensure to cover at least the following aspects in their supervisory assessment:
- a) evaluation of the POG documentation, including a structured pricing process and complexity analysis;
 - b) the process to assess value for money is clearly identified in the manufacturers' POG policy for unit-linked products;
 - c) costs and charges are properly identified in the POG documentation, quantified and due;
 - d) adequate and sufficient testing has taken place on whether the product offers value for money for the target market through its lifetime;
 - e) costs and charges, performance, guarantees, coverage and the services offered are regularly reviewed and *ad hoc* triggers are also sufficiently identified;
 - f) product complexity and target market granularity are explicitly linked;
 - g) adequate systems and controls are in place to ensure products are not 'mis-sold'.
- 3.25. If a competent authority establishes that a manufacturer's POG process does not properly assess value for money risks for unit-linked products, its supervisory action is expected to include a request for adjustment of the POG process, where necessary, and a review of the product based on the revised POG process.
- 3.26. The revision of the POG process and subsequent revision of the product - to be carried out by insurance products manufacturers - can result in:
- a) adjustments of costs and charges;
 - b) an improvement in the benefits offered or services provided including a change of the underlying funds;

- c) a review of the target market, with sufficient remedial measures to be taken for existing customers who do not belong to the target market and whose needs, objectives and characteristics are no longer in line with the product's characteristics, in accordance with Article 7(3) of the POG Delegated Regulation.

3.27. Where, as a result of the supervisory action and a revised POG process, it emerges that the product may have adversely affected customers, in line with Article 7(3) of the POG Delegated Regulation, competent authorities should request manufacturers to take adequate measures, including an assessment of obligations towards the customers to mitigate the situation.

3.28. In performing their assessment of whether manufacturers follow a POG process to ensure that products offer value to the identified target markets, competent authorities should also consider whether there are products which - because of their characteristics and features, including the unbalance between potential losses and benefits or the lack and opaque cost structure - are not suitable to any target market. In this case, competent authorities should consider all appropriate measures under national and Union law to prevent further detriment, including the use of product intervention powers as granted under the Regulation (EU) No 1286/2014.⁹

3.29. Competent authorities are encouraged to communicate good and poor practices to the market and the public, which should assist in acting as a deterrent against unit-linked products with poor value for money.

3.30. This Supervisory Statement will be published on EIOPA's website.

Done at Frankfurt am Main, on 27 November 2021.

[signed]

For the Board of Supervisors

Petra Hielkema

Chairperson

⁹ Regulation (EU) No 1286/2014 of the European Parliament and of the Council of 26 November 2014 on key information documents for packaged retail and insurance-based investment products (PRIIPs), Article 17.

EIOPA

Westhafen Tower, Westhafenplatz 1

60327 Frankfurt – Germany

Tel. + 49 69-951119-20

info@eiopa.europa.eu

<https://www.eiopa.europa.eu>