<table>
<tr><td colspan="3">Comments Template on
Consultation Paper on the proposal for Guidelines under the Insurance Distribution Directive on insurance-based investment products that incorporate a structure which makes it difficult for the customer to understand the risks involved</td><td>Deadline
28 April 2017
18:00 CET</td></tr>
<tr><td>Name of Company:</td><td colspan="3">DAV - German Actuarial Society</td></tr>
<tr><td>Disclosure of comments:</td><td colspan="2">EIOPA will make all comments available on its website, except where respondents specifically request that their comments remain confidential.

Please indicate if your comments on this CP should be treated as confidential, by deleting the word Public in the column to the right and by inserting the word Confidential.</td><td>Public</td></tr>
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<tr><td>Reference</td><td colspan="3">Comment</td></tr>
<tr><td>General Comments</td><td colspan="2">Criteria should be high level and in line with minimum harmonisation aim of</td><td></td></tr>
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IDD

The German Actuarial Society (DAV) agrees that complex products should not be distributed without the appropriatness test. We would like to point out that some product features might be uncommon in one Member State but they can be typical and well-known to customers in another market instead. Therefore, we support that EIOPA envisages only high-level criteria for non-complex products, so that products that are well-known and well understood by consumers in some markets are not wrongly deemed complex. We also welcome that EIOPA acknowledges IDD's minimum harmonisation aim as well as the fact that for execution-only sales national competent authorities may maintain or introduce additional more stringent national provisions in this area in order to protect consumers accordingly.

Level playing field between UCITS funds and collective investment should be ensured

Further from an actuarial point of view, there is no reason why an insurance company's general (cover) assets in which retail investors do not invest directly should be generally regarded as more complex than their UCITS funds counterpart. According to the currently suggested criteria this is due to the fact that insurers also invest in assets that, for example, do not qualify as non-complex products according to MiFID II, such as many long-term investments.

In additition, the required mandatory investment guarantee for products qualifying for article 30(3)(a)(ii) should in our opinion additionally take into account if the underlying investment vehicle itself was not managed according to the general principles that protect customers and limit downside risk to a certain extent. These investment principles could be based on the idea of e.g. ensuring the security, quality, liquidity and profitability of the underlying investment vehicle as a whole. If these principles – that could further be aligned with Solvency II requirements – were fulfilled, the mandatory guarantee requirement should be waived to ensure a level playing field on the notion of product complexity between banks, asset managers and insurance

	companies. **<u>Broader scope of complexity should be taken into account</u>** Moreover, the question if an IBIP qualifies as complex or not is of a great relevance. Not only does it play a role in a so-called "execution-only" distribution of insurance-based investment products (IBIPs), but it is also (presumably much more) relevant in other fields. For example, according to the newly amended PRIIPs RTS complex products according to IDD's scope will then also receive a mandatory comprehension alert. We fear that some products will be unintentionally stigmatised. Many products which are no more complex from a consumer perspective than UCITS funds might be labelled complex just because they fall under a different legal framework and are not covered by MiFID. **<u>The delegated act should take into account changes in the guidelines</u>** Furthermore, the DAV strongly supports that EIOPA will take into account any differences between the delegated act which are currently being finalised by the European Commission and EIOPA's technical advice, prior to finalising these Guidelines. In our view, it is of utmost importance that a consistent approach between Level 2 and Level 3 regulation is ensured such that products that are readily understood by consumers were not wrongly deemed complex. Moreover, although we understand that the distinction between products which fall under Article 30(3)(a)(i) and those that fall under Article 30(3)(a)(ii) originally stems from the IDD Level 1 text, we support that EIOPA is taking a generalised approach to capture the properties of all IBIPs at once.	
Question 1	DAV urges EIOPA to treat complexity in a much broader context. Not only does it play a role in a so-called "execution-only" distribution of IBIPs, but it is also (presumably much more) relevant in other fields. For example, according to the newly amended PRIIPs RTS complex products according to IDD's scope will then also receive a mandatory comprehension alert. We fear that the products will be unintentionally stigmatised. Moreover, also the POG rules newly introduced in the IDD currently	

	depend on the complexity of an IBIP. EIOPA states that the scope and objectives of the proposed guidelines on products' complexity were on facilitating "*the identification of types of insurance-based investment products, or product features within insurance-based investment products, that incorporate structure which makes it difficult for the customer to* ***understand the risks involved*** *and* ***which are therefore complex*** *and* ***not fit for distribution*** *via* ***execution-only***;". Thus, the DAV urges EIOPA to acknowledge that the notion of "product complexity" (and hence not being fit for execution only according to IDD) will presumably have a very high impact on IBIPs through other existing regulations. Thus, absolute care has to be taken in order to avoid postulating principles (by means of Level 3 guidelines) which may leave products that have been established, understood and very well-known to many European insurance markets – such as life-insurance products with profit participation – as being deemed complex under IDD and hence suffer from this notion of complexity in a very different context. For this reason, the DAV does not agree with EIOPAs assessment that IBIPs are "often complicated and difficult to understand for consumers". In our view, especially the principles stated in the consultation paper's guidelines have to be scrutinised thoroughly, especially taking these possible side effects into account.	
Question 2	In our opinion, regardless the additional demands and needs test, execution only sales might currently play a minor role in some markets. However, especially considering the generation of "digital natives", the internet could become a more important sales channel for insurance-based investment products. While it is possible to give advice online we also expect rising demand for execution only sales from digital natives. Therefore, it is important that the demand and needs test does not impede the execution-only distribution of IBIPs. Summarising, in the mid- to long-term the market share of products distributed by means of execution-only may tremendously grow. This potential market growth however implies a thoroughly elaborated approach on the definition of "product complexity" and the demands and needs test now.	

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	Finally, the DAV urges EIOPA to treat complexity in a much broader context than the mere question of execution-only sales of these products. Other possibly far more reaching consequences should be taken into consideration. For example, complex IBIPs will be labelled with a comprehension alert under PRIIPs Regulation, which originally had a much narrower scope for products which cannot be sufficiently comprehensibly described through the PRIIPs KID. Furthermore the complexity of products is a key factor with regard to the scope of the obligations proposed by the current technical advice on product oversight and governance.	
Question 3	From an actuarial point of view, there is no reason why an insurance company's general (cover) assets in which retail investors do not invest directly should be generally regarded as more complex for customers than their UCITS funds counterpart. In our opinion, article 30(3)(a)(i) should additionally take into account if the underlying investment vehicle itself was not managed according to the general principles that protect customers and limit downside risk to a certain extent. This article is supposed to address products which provide only direct investment exposure to the financial instruments deemed non-complex under Directive 2014/65/EU. These are investments where consumers make an investment choice themselves and where the investment exposure is, therefore, not absorbed by the expertise of a professional investor who is subject to supervisory regulation. In such cases the financial instruments invested into by the insurer should not be taken into account if the overall investment ensures that there are no hidden risks for consumers. These investment principles could be based on the idea of e.g. ensuring the security, quality, liquidity and profitability of the underlying investment vehicle as a whole as the prudent person principle under Solvency II. This would ensure a level playing field on the notion of product complexity between banks, asset managers and insurance companies.Otherwise investment products covered by MiFID would receive a preferential treatment compared to insurance products.	
Question 4	We understand that Guideline 1 closely follows the requirements of Levels 1 and 2.	

	However we think there should be a level playing field between investment and insurance products. Often the pooled investment contains less risk for consumers than the average UCITS fund. The benefits are easy to understand even if the actuarial calculation itself might appear complicated. We do not agree with the assessment in Guideline 1. Article 30(3)(a)(i) is suppossed to address products which provide only **direct** investment exposure to the financial instruments deemed non-complex under Directive 2014/65/EU. These are investments where consumers make an investment choice themselves. Products where the customer does not make an investment selection and where the investment is done by the insurer and is subject to a very strong prudent person principle should, therefore, be included in Guideline 1. In such cases indirect investments should not be considered separately if the overall investment ensures that there are no hidden investment risks for consumers. This is also the case for UCITS which on one hand may invest in complex instruments such as derivatives but on the other hand are still regarded as non-complex due to the overarching structure. Therefore, (2.14) should only be restricted to those cases where the provider is not subject to the prudent person principle under Solvency II. Otherwise investment products covered by MiFID would receive a preferential treatment compared to insurance products which are not covered in the MiFID II. Furthermore, the current provisions would also influence the investment of insurers, e.g. impede the investment in alternative investments such as infrastructure. This would go beyond the scope of a Directive on distribution of insurance products. Furthermore, EIOPA notes itself that products with profit participation shemes may provide additional benefits to consumers and seems keen on the further development of collective profit sharing schemes: Gabriel Bernardino says in his speech at the Finanstilsynet Conference: “Pensions when the guarantees disappear” from 9 March 2017: « Products could allow the pooling of investments with the smoothing of returns across members of the pool, so that all members benefit from average long-term returns of the fund and are protected from extremely negative outcomes in stressed market situations. » This statement conflicts with the envisaged notion of complexity.	

Question 5	We support that EIOPA thoroughly investigates different features of IBIPs that might lead to unexpected hidden risks for consumers. However, particularly in view of life insurance products with profit participation it should be duly taken into account that some Member States already implemented rules that protect consumers' interests. (For example, in Germany there are provisions on actuarial calculation of the surrender value of IBIPs. They ensure that consumer receives the right value of his assets in case of an early surrender by demanding that the surrender fees are agreed, put in figures and appropriate. Furthermore, additional rules also exist for allocation of surplus to consumers to ensure strong protection for the customers.) Thus, from consumers' perspective, it is not necessary to understand the exact actuarial methods behind products with profit participation as long as these methods are not arbitrarily set by the manufacturer and follow some law that ensures high level of consumer protection. We would strongly welcome EIOPAs clarification in this regard in guideline 2. **Guideline 2, paragraph 3, (a) to (c)** We strongly suggest that the respective subcriteria (i) to (iii) of criteria (a) to (c) in Point 3 of Guideline 2 should be conclusive and not only conceived as examples of other possible cases of complexity. With a view to the very broad wording of criteria (a), (b) and (c) (without regard to the respective subcriteria), the aim of achieving legal certainty for manufacturers, distributers and consumers alike will otherwise not be achieved. For example the material content of Point 3 (a) of Guideline 2 is limited to the tautology that a product is complex if there are complex mechanisms that determine its payout value. EIOPA should bear in mind that the Guidelines can be amended at any time in the future, should the criteria prove not to be sufficient. **Guideline 2, paragraph 3(a)(i):** We would like to draw EIOPA's attention to the fact that products which offer guarantees almost always provide for a surplus participation of the policyholders. Although confined by strict regulation when apportioning the surplus, the insurer has some leeway in order to balance the individual and the	

	collective interest of policyholders over the long term. We strongly support EIOPA's view, as expressed in the Technical Advice under IDD and reaffirmed in the Consultation Paper, that guarantees are valuable for the customer and should therefore not automatically be penalised by the label of complexity. To ensure high levels of consumer protection, the profit participation is strongly regulated and follows prescribed legal rules (under German law for example Section 153 Insurance Contract Act (VVG); Sections 139 and 140 Insurance Supervision Act (VAG); Sections 6, 7 and 8 Minimum Allocation Regulation (MindZV)). Some rules set by the legislator may in some cases appear complex, but they solely serve best possible consumer protection and should not lead to products being deemed complex. *The following change is necessary:* *(i) the maturity or surrender value or pay out upon death is dependent on* ***profit participation which is not subject to policyholder protection regulation or*** *variables* ***arbitrarily*** *set by the insurance undertaking, the effects of which are difficult for the customer to understand;* **Guideline 2, paragraph 3(a)(ii)** We do not understand why this criterion is relevant for insurers. We assume that the criterion is not aimed at the mechanisms which form the basis of any collective investment: Mr. Bernardino described such products as a candidate for PEPP, which cannot be seen as complex ("Products could allow the pooling of investments with the smoothing of returns across members of the pool, so that all members benefit from average long-term returns of the fund and are protected from extremely negative outcomes in stressed market situations."), see our comments on question 4. Neither are unit-linked products captured by this criterion. → *This criterion should be deleted.*	

	Guideline 2, paragraph 3 (a) (iii): The point that "the maturity or surrender value or pay-out upon death may vary frequently or markedly at different points of time over the duration of the contract either because certain pre-determined threshold conditions are met or because certain time-points are reached" could be interpreted as deeming products with profit participation complex, when they for example guarantee to pay a final bonus on maturity. If contractual dates are clear to the customer at outset this would not seem to be a feature that would be difficult to understand. → *Therefore, we believe this point should be deleted.* **Guideline 2, paragraph 3 (b)** We do not understand why this criterion is necessary. All IBIPs will fall in the scope of the PRIIPs Regulation and, therefore, will provide a KID that describes all the costs included in the product through the disclosure of total costs and the Reduction in Yield (RIY). In particular, the RIY is a new concept that was thoroughly investigated in the consumer testing and is able to present the cost impact in a clear and comprehensive way. → *This criterion should be deleted.* **Guideline 2, paragraph 3 (c)** We understand that EIOPA wishes to keep the surrender fees as simple as possible. However, a too simplistic referece value would not always be fair towards consumers. For example, a fair processing fee of surrending a contract would result in a fixed monetary sum. However, the loss of liquidity premium is fairly measured as a procentage of the investment. Thus, a combination of the in 3(c) mentioned quantities should also be allowed. →*Therefore, the criterion should be amended in the following way* *(c) There are surrender fees that are difficult for the customer to understand,*	

including where the cost of redeeming the insurance-based investment product before maturity does not satisfy one ***or the combination*** *of the following conditions:*

(i) it is a fixed sum;

(ii) it is a fixed sum for each year or other specified time period remaining until the maturity of the contract;

(iii) it is a fixed percentage of the amount of premiums paid or another amount that can be understood by the customer;

(iv) it is a compensation for paying also the part of the surrender value which is greater than the death benefit at the time of surrender.

Furthermore, we would welcome the following clarification of paragraph 2(a):

Guideline 2, paragraph 2a

We agree with the general requirement in Guideline 2 that products which include "*a clause, condition or trigger that allows the insurance undertaking to materially alter the nature, risk or pay out profile of the insurance-based investment product"* shall be deemed complex if these clauses can actually be exercised arbitrarily by the product provider and no further control mechanisms are in place to avoid any consumer detriment.

Guideline 2, paragraph 2(a) A clarification of EIOPA's understanding of "materially altering the pay out profile" of a product would be very much appreciated. Typically, in our view a product's pay out profile might be "materially altered" when clients e.g. at some point in time received an asset they originally had not purchased instead of a monetary cashflow the product was originally equipped with or if clients received the lower value of an asset earlier than the original maturity dependent on a trigger (e.g. compare the possible pay out profile of a convertible bond). In contrast, regarding products where clients "just" receive more or less (monetary) return due to ordinary capital market fluctuations and hence potentially lower surplus participation rates, should not qualify as "materially altering the pay out profile". Hence, we would be grateful if EIOPA clarified the understanding of "materially altering the pay out profile"

	as altering the structure of the pay out (and not the value of return due to ordinary capital market fluctuations) in the guidelines' explanatory text, e.g. by providing some further examples. Further, especially considering long-term business such as life insurance business, some additional clauses in the products' terms and conditions are necessary to ensure that these products will actually work for the considered long-term time frame. Note, if for example a unit-linked policy were not issued with some clauses to replace an underlying investment fund with a similar (but different) investment vehicle, if the corresponding asset manager e.g. liquidated the original investment fund, no long-term product could be offered at all. Therefore, we propose a clarification of the rather general statement of paragraph 2(a) and would appreciate if EIOPA pointed out that only those clauses and conditions whose possible exercise is at the product provider's very discretion shall be deemed complex. If appropriate and hence necessary clauses are formulated transparently in a way that is understandable for the customer, theses clauses shall not yield a product being deemed complex instead.	
Question 6	To our current understanding the definition of complexity and non-complexity following article 30(3)(a)(i) and 30(3)(a)(ii) ("other non-complex insurance based investment products") only differs in the required investment guarantee when "other non-complex insurance-based investment products" are considered. From an actuarial point of view, there is in a first instance little reason why e.g. a non-structured UCITS fund (which is deemed non-complex under MiFID II) shall be deemed non-complex whereas a life insurance product with profit participation – a product family offered in many European countries – shall be deemed complex only due to the presumably lacking but required investment guarantee and because the respective general (cover) assets were not held in a UCITS wrapper although the insurer's general assets aim at (collectively) protecting retail customers in a very similar way as required for UCITS funds. In our opinion, this required mandatory investment guarantee for products qualifying for article 30(3)(a)(ii) should additionally	

	take into account if the underlying investment vehicle itself was not managed according to the general principles that protect customers and limit downside risk to a certain extent. This article is supposed to address products which provide only direct investment exposure to the financial instruments deemed non-complex under Directive 2014/65/EU. These are investments where consumers make an investment choice themselves and where the investment exposure is, therefore, not absorbed by the expertise of a professional investor who is subject to supervi-sory regulation. In such cases the financial instruments invested into by the insurer should not be taken into account if the overall investment ensures that there are no hidden risks for consumers. These investment principles could be based on the idea of e.g. ensuring the security, quality, liquidity and profitability of the underlying investment vehicle as a whole as the prudent person principle under Solvency II. This would If these principles – that could further be aligned with Solvency II requirements – were fulfilled, the mandatory guarantee requirement should be waived to ensure a level playing field on the notion of product complexity between banks, asset managers and insurance companies.Otherwise investment products covered by MiFID would receive a preferential treatment compared to insurance products.	
Question 7	Once again, we want to highlight that the definition of product complexity in the original context of IDD and hence its relation to the execution-process only is most likely to be adopted by different current regulations as well. Hence, although question 7 “only” addresses the issue that products currently already distributed by means of execution-only, may not be fit for this type of distribution after IDD is actually in place, the more pressing question is what the even further consequences of a product being deemed complex rather were? These further consequences have to be thoroughly taken into account when defining the notion of complexity.	
Question 8	<u>Comments on the product examples:</u> Product example 3 is a variable annuity product. The guaranteed surrender or maturity value is hedged using derivative financial instruments in which the customer	

	is not invested. Properly, such a product is considered non complex. However, there are also constructions in which the fair value of the guaranteed benefits is part of the surrender or maturity value. This fair value is the sum of fair value of the non-structured UCITS and the derivative financial instruments. Such a product would be classified as complex because the derivative financial instruments are complex. This product design carries the same risk as the product above but the customer benefit is significantly higher in this product. Such contradictions must be avoided. Example 3 can also be built as an insurance-based investment product where the customer does not make an investment selection. The insurance undertaking guarantees that the surrender or maturity value is at least 80% of the premiums paid by the customer. The product does not have any other structures which make it difficult for the customer to understand the risks involved. If, however the insurer invests in derivatives to provide the guarantee, the product is deemed complex under Article 30(3)(a)(i) and (ii) (see Example 9). In addition, we would like to note the following: This example shows that product features that benefit consumers are classified as complex. If such schemes were removed, the product would be no longer classified as complex, however, the benefit for consumers will be reduced. Such contradictions must be avoided. EIOPA states that product example 9 shall be deemed complex. In contrast, product example 7 shall not be deemed complex. Example 7 and 9 only differ by a potential investment in derivatives by the insurance company which then yields product example 9 being complex. We want to sincerely stress that the sheer existence of a potential derivative investment structure cannot mandatorily leave an insurer's product being complex. If so, each (structured and non-structured) UCITS fund – which could potentially invest into some derivatives as well – should also be deemed complex. However, this notion of complexity would then contradict MiFID II. Therefore, product example 9 shall in our view (similarly with a UCITS fund) not be deemed complex in general only due to the possible existence of derivative instruments and due to the offering by an insurance company instead of an asset manager via a UCITS fund. In order to ensure a level playing field of different product	

	providers (here: insurance companies and asset managers), a level definition of the notion of complexity shall be reached. EIOPA acknowledges that life insurance policies with profit participation shall not in general be deemed complex by describing product example 11. However, combining product example 11 and the proposed paragraph 3(a) of guideline 2 eventually leaves product providers with a very incomplete picture of what and if so which kind of profit sharing mechanism shall actually be deemed complex or not. Therefore, we strongly propose EIOPA to amend paragraph 3 of guideline 2 – following product example 11 – such that profit sharing mechanisms do not generally yield to complex products. A possible solution could be that only profit sharing mechanisms where products providers may arbitrarily exercise these discretionary participation mechanisms should be deemed complex.	
Question 9	The DAV strongly supports that EIOPA will take into account any differences between the delegated act which are currently being finalised by the European Commission and EIOPA's technical advice, prior to finalising these Guidelines. In our view, it is of utmost importance that a consistent approach between Level 2 and Level 3 regulation is ensured so that products that are readily understood by consumers were not wrongly deemed complex. Furthermore, the question of complexity of IBIPs is of a great relevance. Not only does it play a role in a so-called "execution-only" distribution of IBIPs, but it is also (presumably much more) relevant in other fields. For example, according to the newly amended PRIIPs RTS complex products following IDD's scope will then also receive a comprehension alert. From an actuarial point of view, there is no reason why an insurance company's general (cover) assets in which retail investor do not invest directly should be generally regarded as more complex for consumers than their UCITS funds counterpart. According to EIOPA's current interpretation this is due to the fact that insurers also invest in assets that, for example, do not qualify as non-complex products according to MiFID II, such as many long-term investments. The current text	

	yields to an unlevel playing field between different product providers such as fund managers and insurers.	