

*As the year starts, it is “all change” in terms of the make-up of the EU Commission. Yet as a new team of Commissioners takes office the subject matters under the spotlight and the work programmes ahead remain much the same as at the end of 2009. M Barnier, the new Internal Market and Services Commissioner, has already made it clear that “... no market, no financial player, no product, no territory should be able to escape anymore relevant regulation and effective oversight”. His main objective in 2010 therefore is to implement the financial reform package agreed by the EU Council of Ministers at the end of 2009 which at present is undergoing discussion in the European Parliament.*

*Further down the list of priorities this coming year is EC consultation on a proposed common regime on the sale and disclosure of packaged retail investment products, the drafting and adoption of the Solvency II implementing directive, further initiatives on pension transfers and a review of the MiFID directive. Underlying all these activities will be a key driver to advance the power of the consumer, evidenced most recently in the published results of an EC study on tying and other potentially unfair commercial practices in the retail financial services sector and further prospective moves to outlaw personal discrimination.*

*This edition brings readers up-to-date with the latest developments.*

### **New financial regulation**

The EC package on financial regulatory reform was adopted by EU Council of Finance Ministers (ECOFIN) at beginning of Dec. and now awaits the agreement of European Parliament (EP), under ‘co-decision’ procedure. This next stage is likely to be complex and protracted as MEPs are known to favour even stronger supervision and the whole process is expected to take up to 6 months involving no less than five different MEP rapporteurs (including Peter Skinner UK MEP who guided the Solvency II framework directive through the EP).

As it stands, the package is built on twin pillars of European Systemic Risk Board (ESRB), operating from Frankfurt under auspices of European Central Bank, and European System of Financial Supervision (ESFS), encompassing three new European Supervisory Authorities (ESAs) replacing the existing Lamfalussy technical committees (CEBS, CESR and CEIOPS) for banking, securities and insurance. The ESRB’s only power will be to issue major financial risk warnings and recommend action while the ESAs will have wider powers over national regulators than hitherto, for example, in prescribing binding technical standards (‘single rulebook’).

The UK Government has indicated its broad support for the new financial architecture but with scope for amendment and improvement in certain areas. In particular, it believes that whilst ESAs should ensure the consistency and quality of national regulators, day-to-day supervision of firms is better undertaken at the national level. This is largely because:

- national supervisors are closer to the market and therefore better able to judge the impact of prudential supervisory decisions; and
- national governments remain responsible for any fiscal support to firms – there is no equivalent EU mechanism that could provide the fiscal support necessary to support the financial sector – therefore supervision must remain accountable to national parliaments.

Elsewhere, the UK Government wants to limit the scope of ESAs in exercising direct supervisory powers over entities with Community-wide reach to credit rating agencies only and should not be able to direct individual national supervisors over individual firms, given that Member States are responsible for crisis management and resolution. ESAs should nonetheless play a strong co-ordinating role in a crisis.

It also believes that ESAs should not be allowed to request information directly from firms and that in the interests of transparency and avoiding excessive administrative burdens it is preferable that ESAs should only receive regular information via national authorities, and subject to the principles of proportionality.

Finally, the UK Government is keen to limit the influence that the EC Commission has over the workings of the new agencies (both the ESRB and ESAs) and that clear dividing lines be drawn to ensure their relative independence.

It remains to be seen how much of an UK approach MEPs are prepared to take in debating the finer elements of the reform package.

### **Packaged retail investment products (PRIPs)**

At an EC workshop held in October with EU regulatory and trade bodies, the EC re-affirmed its intention to press ahead with formulating a horizontal approach to selling and customer disclosure practices on packaged retail investment products. A full consultation paper is expected to be issued early in 2010.

Amongst the findings from the workshop was a realisation of the need to reflect the right balance to reflect differences between different investment products and services. Otherwise, any attempt at maximum harmonisation may only serve to stifle financial innovation and development to the detriment of consumer interests. Key considerations therefore remain focused on the scope of any new measures and the boundary between PRIPs and non-PRIPs, such as certain types of traditional and with-profits life insurance contracts and certain kinds of pensions and annuities. At the workshop, the European Insurers Federation (CEA) supported the inclusion of with-profits and index-linked, but not traditional, life policies but against including pensions and pension annuities.

On pre-contract disclosure, there was some consensus towards adopting a Key Investor Document, initially being tested for UCITS products, to PRIPs though with scope for variation in respect of insurance products where it might not be wholly

appropriate - as observed by a CEIOPS representative. In particular, past performance and risk data may be difficult to present in a meaningful manner across a range of products suggesting the use of a 'traffic light' system for different products.

On selling practices, the EC re-affirmed its position in favour of adopting a MiFID-style approach particularly in respect of the duty of the advisor to assess the suitability of any product being recommended for the investor and the conditions put on intermediary remuneration, including effective disclosure so that investors are aware of commissions paid. This approach seemed to command general support, at least in principle, although in an interesting side-observation, AILO (Association of International Life Offices) noted that in Finland, as a consequence of fee-based remuneration being introduced to replace commission payments, independent intermediaries were becoming tied agents to the detriment of consumers.

An update on the EC's work on PRIIPS, including results from the workshop, can be viewed on [http://ec.europa.eu/internal\\_market/fin services-retail/docs/investment\\_products/20091215\\_prips\\_en.pdf](http://ec.europa.eu/internal_market/fin services-retail/docs/investment_products/20091215_prips_en.pdf)

ILAG has also produced its own unofficial Q/A paper on PRIIPs which can be obtained from [doug.thow@ilag.org.uk](mailto:doug.thow@ilag.org.uk)

### **Tying and unfair commercial practices**

The EC has recently published an independent study report on tying and other cross-selling commercial practices in retail financial services for consultation. The report found that cross-selling practices, of which tying represents about one-third, and conditional sales practices are widespread in the EU and also concludes that mortgages, consumer loans and bank current accounts take a leading role as gateway products for cross-selling practices.

According to the study, the main reasons for financial institutions to engage in cross-selling practices are commercial strategy, risk reduction and cost efficiency. Consumers are seen as having no choice but to purchase products that are tied or subject to conditional access. However, many of these practices are deemed anti-competitive in reducing customer choice and availability, price transparency and the comparability of market providers.

The study suggests that a total number of 572 m. contracts could be switched if practices at hand, in particular cross-selling and conditional practices, were not applied by financial service providers. The effects are felt differently in Member States with only twelve Member States having adopted specific solutions, some of far-reaching prohibitions. However, even in those Member States where tying is officially banned, bundling replaces it with practically the same effects.

Much of the focus of the report is on banking practices though insurance is also mentioned in the context of life policies sold with mortgages and payment protection taken out on goods and services. Overall, the UK comes out with a relatively clean bill of health even though tying and bundling are not specifically banned other than where they fall under competition law or statute law implementing the EC Unfair Commercial Practices Directive. The report also notes that several retail financial markets – most recently, personal current accounts and PPI policies – have been periodically and extensively monitored and scrutinised in the past few years.

In the consultation paper, the EC seeks feedback from stakeholders as to whether in the light of the reports' findings as to variations in Member State law and practice, it

should introduce EU horizontal legislation or proceed via other measures to protect consumers.

The EC consultation paper and study report can be accessed via [http://ec.europa.eu/internal\\_market/consultations/2010/tying\\_en.htm](http://ec.europa.eu/internal_market/consultations/2010/tying_en.htm)

### **Feedback on banning age discrimination in EU**

In a recent feedback statement published by the UK Government Equalities Office (GEO), there is general support from the industry for a legal exemption to allow financial service and insurance providers to price products variably, according to age and disability, provided that it can be substantiated by authoritative data.

Financial services respondents, including ILAG, said that not allowing age and disability to continue to be determining factors of risk in the industry would harm both consumers and businesses. Age and disability were legitimate factors taken into account when giving advice on products such as investments, equity release, and pension accumulation. Otherwise it is argued that premiums could rise across the board to pay for the increased risks to the disadvantage of lower-risk consumers.

The current exemption contained in the draft EC Equal Treatment Directive allows for proportionate differences in treatment where, for the financial service in question, the use of age or disability is a determining factor in the assessment of risk based on relevant actuarial principles, accurate statistical data or medical knowledge. The industry has therefore sent a strong message to the UK Government that it wishes to see this retained although there was less accord amongst equality groups in the feedback received who felt that the exemption as drafted would allow discrimination to continue as stereotyping was widely used in financial services.

The EC directive is still under negotiation in Brussels but it is hoped to reach final agreement under the EU Spanish Presidency over the first six months of 2010. The final text will also be critical in terms of influencing the timing of implementation of similar provisions in the UK Equality Bill which is currently before Parliament.

The GEO feedback statement can be accessed on <http://www.equalities.gov.uk/pdf/Acc%20summary%20of%20responses.pdf>

*End.*

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