Submission on Central Bank of Ireland Discussion Paper on the Payment of Commission to Intermediaries

Zurich Life Assurance plc

Summary

In general, we believe that the current commission model, and Consumer Protection Framework, serve customers well. In the Irish market we observe the following points which provide evidence to support the effectiveness of the current regime:

- There is widespread access to advice, with independent advisers available to all sections of society throughout the country
- There is little evidence of product overselling, or mis-selling
- There is strong competition in both the life and non-life sectors, with a wide variety of distribution models and products
- There are low levels of upheld complaints, based on Financial Services Ombudsman data, with total compensation payments paid of less than 0.01% of premiums written.
- There are high levels of persistency on life insurance and pension products, indicating customers are satisfied with the products they have been sold

Significant restrictions on commission or other fundamental changes to the market are likely to have a detrimental impact in the following areas:

- It will reduce the availability of advice by restricting its supply (as already seen in the UK market)
- It will increase the overall cost of advice, and make advice unaffordable to those who most need it (lower income customers who cannot afford to pay a direct fee)
- It will reduce levels of insurance and pension coverage
- It will increase the risk of product mis-selling. Globally, mis-selling has typically arisen where product providers have pushed products on their customers through direct sales without independent advice.
- It is likely to result in less competition and higher customer charges over time

As well as these clear detrimental impacts, we cannot see any potential for significant restrictions on the current commission model having a positive impact on customers. However, we do believe that there are potential areas where the existing framework could be improved:

- Consideration should be given to requiring providers to ensure that consumers sign a warning/waiver where independent advice has not been provided, and the consumer is therefore very unlikely to have purchased the best value product
- There should be consistency between commission disclosure requirements on similar products (e.g. the disclosure requirements on life insurance products, investment products and pension products should all be identical)
- Consideration should be given to widening the areas where commission disclosure is compulsory, to include all types of investment and pension products (whether owned by a company or an individual)
- Consideration should be given to introducing a requirement for advisers to detail the annual services provide by the adviser, where the adviser is earning an ongoing commission

- Consideration should be given to not allowing advisers to earn a commission from multiple sources from one product (e.g. it should not be possible to earn a commission on a product, as well as on an investment held within the product).
- Override commission which is linked to business volumes should not be allowed on complex products (i.e. life insurance, pensions, investments)

1. In your view, what aspects of how intermediaries are paid commission work well to deliver responsible business conduct, fair treatment of consumers and avoidance of conflicts of interests when consumers are sold financial products?

The existing commission model in the Irish market allows intermediaries to offer flexible options to customers, in terms of how advice is paid for. It also allows access to advice for all types of customers, and avoids the risk that customers will be unwilling to seek advice on financial matters because of a need to pay a direct fee.

The Consumer Protection Code provides a good and comprehensive framework to ensure fair treatment of customers, and our experience is that intermediaries are very aware of their obligations under the Consumer Protection Code. In addition, the Life Insurance Disclosure Regulations provide strong transparency for customers on the commission payments and charges on more complex life insurance products.

2. In your view, what aspects of how intermediaries are paid commission do not succeed in delivering responsible business conduct, fair treatment of consumers and avoidance of conflicts of interests when consumers are sold financial products, or present particular risks in this regard?

Overall, we believe that the current commission model, and supporting Consumer Protection Framework, is proven to work well. We do not believe there is any material area where the current framework has not succeeded in delivering the points mentioned.

3. In your view, are there any changes needed to commission arrangements in Ireland, regulatory or otherwise, to do more to encourage responsible business conduct, fair treatment of consumers and avoidance of conflicts of interests when consumers are sold financial products?

We have highlighted some potential areas for improvement in our summary on page 1 above.

4. Are there other features or types of commission arrangements that the Central Bank should take into account in considering this topic?

The Central Bank has comprehensively described the range of commission structures available in the market across all types of products. When stating the commission rates available on Life Assurance products, we note that the Central Bank has stated the maximum rates available in the market. We note that it would be highly unusual for the maximum rates of all types of commission to be paid on one policy, and the typical rates paid would be much lower than the maximums stated. We also note that, in some circumstances, commission may be paid on 2 parts of a product sale. For example, commission may be paid on sales of a life insurance pension product, as well as on the structured deposit in which the product invests. We believe consideration should be given to not allowing commission payments from multiple sources arising from one product sale.

5. Are there practices or features of commission arrangements in other jurisdictions to which you think the Central Bank should have regard to?

By international standards, we believe the commission disclosure and Consumer Protection Framework is strong. For example, the commission disclosure requirements in the Life Insurance Disclosure Regulations are as comprehensive as any we have seen elsewhere.

6. Are there any changes to these practices which you consider necessary or appropriate to better promote responsible business conduct, fair treatment of consumers and avoidance of conflicts of interests when consumers are sold financial products?

We do not think that any fundamental changes are required to the commission arrangements in Ireland. We do think the regime could be enhanced in certain areas, as set out in the summary on page 1.

7. Are there features of the current consumer protection framework that you would highlight as strengths in the context of commissions specifically?

In general, we believe the current consumer protection framework is comprehensive and, in our experience, advisers are very aware of their obligations under the framework.

We believe the product suitability element of the framework is the key are, and the requirement to provide a written statement of suitability on each sale is an important strength of the framework.

8. Are there weaknesses or gaps in the current consumer protection framework in the context of commissions specifically?

There are some potential areas for improvement, as set out in our summary on page 1.

9. Do you have any other observations on the current domestic framework as it relates to the practice of paying commissions in Ireland?

No other observations.

10. Do you have any general views on the potential benefits to consumers of properly designed commission structures outlined in this section?

The Central Bank has comprehensively described the potential benefits of properly designed commission structures. Access to advice is an important issue, and we note that initial findings after the introduction of RDR in the UK suggest a large reduction in the number of advisers, and inevitably less access to advice.

Advice has been an important driver of participation in financial service in Ireland. We note that 70% of pension sales are through brokers, and it is clear that pension coverage in Ireland would be much lower in the absence of brokers who are incentivised to encourage people to save for their retirement. In relation to paying an upfront fee for advice, we believe there is strong evidence in the Irish market that customers would be reluctant to do so: independent advisers already offer customers this option, but there is very little take-up of it – in other words, customers prefer a commission model over direct fees, when given the choice.

11. Are you aware of any additional potential benefits to consumers? If so, please describe them.

We believe that commission is the only way to support an independent advice model: In the absence of commission, it would be very difficult for an independent advice model to be made available to all customers. As such, it is likely than more sales would be done directly with product providers. We note that the mis-selling scandal of payment protection insurance in the UK and elsewhere took place largely through direct providers. In the absence of widespread access to independent advice, there is a much heightened risk of product mis-selling by providers through direct or tied distribution. In addition to a higher risk of mis-selling, reduced availability of independent advice is likely to result in consumers purchasing higher cost products, as they will no longer have the services of a broker who will be able to search the market and select the best product.

12. Have you observed any of these potential benefits? If so, please provide examples and describe the kind of benefit that has accrued.

In relation to product suitability, we believe the high levels of persistency in the life insurance/pensions market are strong evidence that customers are being sold suitable products. In addition, the level of claims upheld by the Financial Services Ombudsman, with total compensation of just over €1 million paid to complainants in 2015 across all financial services (banking and insurance), in an industry with annual premiums exceeding €10 billion.

13. Would you weight any of these potential benefits over others as requiring special consideration or attention, and if so why?

We would weight widespread access to advice as the key benefit of the commission model and any changes to the commission model should carefully consider what impact they might have on access to advice.

14. Do you have any suggestions as to how the current regulatory framework could be improved or changed so as to enhance the potential benefits to consumers that arise from the payment of commissions to intermediaries so as to better promote responsible business conduct, fair treatment of consumers and avoidance of conflicts of interest when consumers are sold financial products?

There are a number of potential areas for improvement which we have highlighted in the summary.

15. Do you have any general views on the potential risks to consumers of commission structures outlined in this section?

In general, the Central Bank has provided a comprehensive description of the theoretical risks of commission structures. We note that the Consumer Protection Code and the Life Insurance Disclosure regulations are long-established and, therefore, the focus should be on whether such theoretical risks exist in practice (given the existing consumer protection framework). We believe that there is little evidence that the existing commission model has had any detrimental impact on customers.

16. Do you consider the potential risks to be accurately described? If not, please explain why.

We do not believe that there is a potential risk that a commission model would result in a "higher costs of products". There is no theoretical case for suggesting that restricting the way in which advice fees can be paid would reduce the cost of advice. In practical terms, the UK experience proves that removing commission does not reduce the cost of advice. Restricting the way in which advice can be paid for could only reduce the supply of advice, and reducing the supply of any service can only lead to an increase in the cost of advice. Suggestions in the UK and other markets that "robo-advice" could fill the advice gap at the lower end of the market are a disservice to customers: the least well off are most in need of high quality advice.

In relation to the risk of "fund erosion", we note that there is a requirement to provide an annual statement to customers, and this mitigates the risk that the value will be eroded without the customers being aware of it.

In relation to transparency, the Life Insurance Disclosure regulations require commission to be shown in monetary form, avoiding the potential for customer confusion.

In relation to the risk that no ongoing benefit to consumers is received for ongoing payments, we do not agree that, in many cases, the consumer does not receive any benefit in return for ongoing commission. We are unsure what data the Central Bank has to support this contention. In our experience, advisers provide ongoing advice and service to their customers, both through formal annual reviews and informal discussions. In relation to the Central Bank's specific comments on ongoing commission on term insurance, commission is paid on a spread basis so that insurers and advisers can manage their persistency risks in an equitable fashion - spread commission on term insurance is likely to encourage higher quality sales. In relation to ongoing commissions in general, consideration should be given to requiring advisers to specify the services they provide to customers on an ongoing basis.

17. Are you aware of any additional potential risks to consumers? If so, please describe them.

We are not aware of any other potential risks.

18. Have you observed any of these potential risks at play? If so, please provide examples and describe the impact of the risk?

We have not observed any material evidence that these risks are at play in the area of the market with which we are most familiar (life insurance and pensions sold through independent brokers). In relation to Product and Producer Bias, in practice, the same or similar rates of commission are usually available from multiple providers. In relation to override commission (i.e. commission where a higher rate is payable depending on volumes of business written), this has the potential to lead to poor advice on complex products (life insurance, investment, pensions), and there is a strong case for not allowing it on those products. In relation to overselling, we believe that underinsurance is a much bigger issue than overinsurance.

19. Would you weight any of these potential risks over others as requiring special consideration or attention, and if so why?

We believe the key risk to consider is that customers are sold unsuitable products. We believe there is no evidence this risk has materialised in the Irish market under the current regulatory framework.

20. Do you have any suggestions as to how the current regulatory framework could be improved or changed so as to better manage the potential risks to consumers that arise from the payment of commissions to intermediaries?

We believe that the current regulatory framework provides good protection and transparency to customers. We have highlighted a small number of potential areas for improvement in our summary on page 1.

Zurich Life Assurance plc

18th October 2016