



## European Commission Green Paper on Retail Financial Services

### Response from Prudential plc

#### **Introduction**

1. Prudential plc is a leading international financial services group offering insurance and pensions products, as well as retail and institutional fund management services, with operations in the UK, Europe, the US and Asia. Our EU cross border business is primarily undertaken by Prudential International Assurance and M&G International.
2. Prudential welcomes this Green Paper and the opportunity that it provides for comment on the Commission's overarching policy objectives in the area of retail financial services. We hope that our consultation response will help inform the Commission's understanding of some of the issues that confront both consumers and industry in the field of retail financial services.
3. As a number of the initiatives referred to in the Green Paper are already underway, we have omitted detailed views, as these have previously been submitted on targeted measures such as investment funds, Solvency II and mortgage credit. However, we commend the Commission on this latest initiative to draw together the various strands of its work programme on retail financial services and would welcome the opportunity to further assist the Commission in this policy area going forward.

#### **Key Priorities for Prudential**

4. In order to effectively promote further retail financial services integration, Prudential believes that a focus on the following areas will be essential:
  - *Continued promotion of better regulation* – regulatory interventions will only deliver positive benefits if they are based on a strong economic case and informed by rigorous cost benefit analysis.
  - *Solvency II* – a harmonised and proportionate solvency regime for insurance supervision in the EU is essential to ensuring consumer confidence in the sector.
  - *UCITS reform* – enhancing the efficiency of European fund markets is just one aspect of reform the other is meeting consumer demand for a diversified range of competitive investment products.
  - *Financial literacy* – well-informed and financially literate consumers are essential if a more integrated and sustainable market in retail financial services is to become a reality.

## **General Comments**

### *Context*

5. We would agree with the Commission's view that, whilst much has been achieved to date in creating a single market at the wholesale level, for a number of reasons retail markets, particularly in the life and pensions area, remain largely national. Whilst this means that there may yet be consumer benefits to be realised from greater integration, it is important to recognise that there are many understandable factors behind a lack of integration to date.

6. The reasons for this lack of integration include factors such as language, culture and brand loyalty that have been and will remain largely immune to legislative resolution. In addition the key area of tax treatment remains politically highly sensitive. It is therefore important that there are realistic expectations of the extent to which regulatory interventions alone will drive further integration in EU retail financial services markets.

7. In this context we welcome the Commission's willingness to consider a full range of policy options in pursuing the goal of further integration and the ongoing commitment to the principles of better regulation. In particular the Commission should only undertake new regulatory initiatives where the economic case has been made for intervention and it is clear that the measures will encourage both the industry supply of financial products cross border and stimulate sufficient consumer demand.

8. To that end we would strongly encourage the rigorous use of cost benefit analysis and Impact Assessments when determining the appropriateness of any future regulatory proposals.

### *Meeting consumers' needs*

9. Prudential fully supports the Commission's commitment to removing barriers for retail financial services where this will deliver concrete benefits to consumers.

10. We therefore welcome the proposed CEIOPS review of national 'general good' rules and the Commission's commitment to eliminating any market protectionism, or unnecessary regulatory costs, that unjustified use of these rules may currently impose. Although we do not underestimate the difficulties associated with such a review, it is our hope that through this process, the Commission might be in a position to develop a standard defined set of 'general good' requirements which could be employed by all member states. This would allow both domestic and companies trading cross-border to operate on a level playing field, which should in turn allow for greater competition and increased consumer choice.

11. Notwithstanding our desire to see swift action taken to remove unnecessary barriers to cross-border trade, it remains important that any Commission intervention in retail financial services markets should be fully justified both in terms of consumer demand and strong economic rationale. Careful regard must be given to the impact of any proposals on existing national markets for retail financial products. For instance, in taking forward the proposed Directive to improve the portability of supplementary pension rights, care must be taken to ensure that in delivering greater

cross border pension rights, existing pension markets are not adversely affected, thus damaging consumer interests.

12. In our considered view, a properly integrated retail financial services market will not be achieved in the short term and therefore cross-border trade will continue to be driven primarily through branches in the host market for some time to come. As such, the Commission should seek to ensure that any proposals developed to enhance cross-border trade do not create additional burdens to business conducted through branches.

#### *Innovation/new products*

13. Prudential notes the Commission's intention to undertake a review of existing national regulatory frameworks for equity release products in 2008. We would welcome further clarification from the Commission as to the rationale for this review and its likely scope.

14. In our view, equity release markets are still at an early and innovative stage of development. Consumer needs are still developing and providers are looking to respond to these developing needs. In this context, it will be particularly important to ensure that precipitate action that might distort the market in future is avoided and that a clear business case for intervention has been identified before any action is taken by the Commission. This should help avoid the risk that regulation retards the development of an important new market for consumers.

15. This is an important point to be made more generally in relation to regulatory interventions in retail financial services markets. Where these markets are dynamic and competitive, they will be characterised by product innovation. As such, even where the Commission believes that interventions are justified on economic and cost benefit grounds, great care must be taken in designing regulation so that it is flexible enough to accommodate new products and does not hamper or distort market development.

#### *Enhancing consumer confidence*

16. Solvency II is the most important strategic issue for the insurance sector, particularly in terms of guaranteeing the continued international competitiveness of EU insurance markets. A harmonised and proportionate solvency regime for insurers across the EU is also an essential component of ensuring consumer confidence in the sector. The Commission should therefore prioritise the agreement and implementation of Solvency II over the development of new initiatives in EU insurance markets.

17. We also welcome the Commission's focus on work to improve supervisory cooperation. The delivery of Solvency II will demand significant levels of cooperation between supervisors and will require an appropriate balance between the roles and responsibilities of the supervisors, if it is to be successful.

18. In order to secure consumer confidence, it is important that consistent levels of consumer protection apply across products and across borders. The Commission's proposed reviews of the Distance Marketing and Insurance Mediation directives should help ensure that consumers are provided with effective and consistent protections. However, clear action to amend directives in the wake of

these reviews should only be taken after a full impact analysis that demonstrates the costs of further change to the regulatory regime are outweighed by the benefits that it would deliver.

### *Empowering consumers*

19. Prudential agrees with the Commission that well-informed and financially literate consumers are essential if a more integrated market in retail financial services is to become a reality.

20. We welcome an informed debate around the regulation of information disclosure in retail financial services, through the various reviews and initiatives that the Commission has outlined in this Paper. However, this debate must start from a position of understanding about the ways in which consumers actually behave and make use of the information they are given. It must also be a debate that maintains a clear distinction between provision of information and advice and we are encouraged by the Commission's recognition of this point in the Green Paper. Finally full cost benefit analysis should be undertaken to inform any proposals on information disclosure.

21. In terms of activity in this area, we would suggest that the Commission should focus its efforts on ensuring that there is consistency between EU Directives in terms of the information provisions they contain. A failure to ensure consistency, both in existing regulation and future proposals, risks confusing consumers and generating unnecessary costs for industry.

22. We would also suggest that the Commission would do well to focus on standardising key information requirements based on research as to what will be effective for consumers, rather than seeking to devise detailed scripts around disclosure that prescribes the content and format of documents. As such we welcome the proposal to make use of consumer testing in the context of the UCITS review, in addition to cost benefit analysis work.

23. Differences in the underlying structure of products will also require that a degree of flexibility exists within any disclosure requirements and the more proscriptive the detail of these requirements are, the more difficult it will be to achieve this flexibility.

24. Finally, Prudential whole heartedly endorses the Green Paper's recognition of the importance of improving consumers' financial literacy. Building financial capability has to be the cornerstone of any attempt to empower consumers of retail financial services. This is an area where Prudential has been working hard in the UK and internationally since 2001 and we believe that financial literacy could be effectively supported at a European level by promoting best practice. In particular we believe that the 'partnership' approach by which financial capability has been taken forward by the FSA, industry and NGOs in the UK, is a model that the Commission should look at closely.

**Answers to Specific Question, where appropriate:**

**1) Do you agree with the objectives and priorities set out in this paper?**

Prudential supports the objectives and priorities as set out in the Green Paper.

Please also refer to our earlier comments.

**(2) Are there issues that are not covered in this Green Paper, which are important for the integration of retail financial markets and to which the Commission's attention should be drawn? For example, are consumers in their everyday life confronted with requirements or limitations from either financial services providers or other stakeholders (employers, social security, administrations, businesses, etc.) which restrict their ability to use cross border financial services (such as an obligation to have a bank account or insurance policy in one specific country, etc.).**

Whilst we believe that the Green Paper sets out a comprehensive list of targeted measures that the Commission intends to undertake in future, in line with the principles of better regulation, we would wish also to draw attention to the importance of ensuring proper implementation of measures that have already been agreed. Effective implementation of directives, both in terms of ensuring timely transposition and dissuading individual regulators from super-equivalence, is crucial for the delivery of a level regulatory playing field, which is in turn a prerequisite for a more integrated retail financial services market.

**(3) The Commission has undertaken several initiatives to improve consultation with consumers and to secure their input into its policy making. Should further steps be taken and, if so, what steps?**

Prudential supports the Commission's efforts to solicit the views of all stakeholders and would welcome any further steps to improve engagement. As a general principle we would suggest that the earlier such consultation occurs within the policy development process, the more effective it will be.

**(4) Is consumer choice unnecessarily limited by restrictions on the providers and channels through which they access retail financial services. What are, in your experience, these restrictions?**

The UK enjoys a dynamic and competitive retail financial services market in which savings and investment products are provided through a variety of direct and indirect channels. This ensures that consumers are able to choose from a wide range of products in any given segment of the market and means that they are better able to select those which most closely suit their individual needs.

Prudential would suggest that the Commission should pay particular attention to ensuring that any future proposals for regulatory interventions are carefully assessed against potential negative impact on existing markets.

**(8) The Commission believes that it has an important role to play in developing a competitive, open and effective market for long-term savings, retirement and pension schemes that meet consumers' needs. Do stakeholders agree and how could the Commission contribute? Could an optional legal EU-wide regime ("28th regime") for savings and/or 3rd pillar pension products be envisaged?**

A stable regulatory framework across the EU that encourages growth of long-term savings is clearly important; however the development of markets will primarily be driven by the commercial attractiveness of those markets to both providers and consumers.

Whilst the Commission may have a role to play in removing existing barriers to greater integration of retail savings markets, any further activity in this area should be carefully tested against the principles of better regulation and subject to full cost benefit analysis. The experience of the Pensions Portability Directive clearly illustrates the difficulty of devising common measures without risking unacceptable consequences for member states' existing pension systems.

On the specific question of the "28<sup>th</sup> regime", we have no objection to the Commission exploring this concept further, and the recent paper by the European Financial Services Round Table provides further input on how such a regime might work for a European Pension Product (EPP). Further consideration of this particular product would need to include careful consideration of its financial viability, an assessment of the take up amongst mobile workers and those choosing EPP in preference to other national options. The implications for national markets should also be considered, including how consumers would choose between the increased options available and the regulatory framework which would apply to that choice. As a first step, the Commission might consider setting out a workplan covering the areas which need to be reviewed if the concept is to be effectively evaluated.

It has been suggested that UCITS could act as a model for a 28<sup>th</sup> regime, however, as the UCITS regime does not cover the whole of the value chain and leaves considerable powers with the host regulator regarding marketing, it would be an imperfect model. Any true 28<sup>th</sup> regime would have to cover all aspects of the value chain and to that end UCITS could only act as a starting point for developing such a framework.

***(10) The Commission believes that more could be done to improve consumers' financial literacy and capability. Possible measures include developing guidelines or promoting best practices. The Commission would welcome input on how this policy should be further developed at the European level.***

Prudential welcomes the Commission's Green Paper and is pleased to comment on potential areas to improve consumers' financial literacy and capability, including developing and promoting best practice. Prudential believes that this could be developed further at the European level by examining the work underway in the UK, led by the Financial Services Authority, which has carried out extensive research and piloting work and now has seven priority areas underway both with adults from all socio economic groups, and in schools. In addition, the FSA has just commissioned a review of progress for the seven priority areas, less than a year into the programme and is examining the way forward beyond 2011.

One of the most important messages is that of 'partnership'. No one single organisation can take this forward alone. The UK has had some success in this area due to the joined-up approach of government, politicians, regulator, NGO's and financial services sector. These organisations have come together under the direction of the FSA's Financial Capability Steering Group. A demonstration of this would be Prudential's own financial literacy programme, which has been developed since 2001 through our Corporate Responsibility programme, with the aim of helping people become more informed about their financial needs, building the long-term

capacity of community organisations to provide financial education to adults and children.

Research to establish the breadth and dept of the problem is essential. In the UK, the FSA's Baseline Survey published March 2006 has served to focus on the challenges faced by the lack of financial understanding in the UK. The financial services industry, which is dependent on having educated consumers who make the right choices for their long term financial security, has a vested interest in ensuring that consumers understand what they are buying and even whether or not they should be buying a financial product. The survey also served to highlight the need for better financial education in schools. Prudential believes that this could be strengthened by making financial capability a formal part of all Schools' curricula, not as a standalone subject, but embedded into several important curriculum areas. Financially aware young people will develop into better-informed, financially literate adults.

***(11) Do you think that, as they stand, the provisions on consumer information contained in financial services directives are adequate and consistent with one another? Were it not the case, how could the Commission ensure that information requirements are set at the right level, ensuring proper information but without creating any overload? Do you think that informing consumers is sufficient or that advice should also be provided? If yes, should that be compulsory or on request?***

Prudential welcomes the reference in the Green Paper to the proposed reviews of the Distance Marketing Directive and the Insurance Mediation Directive, in order to assess their effectiveness and to ensure that the information provisions they contain are consistent. In general it is our view that wherever information provisions are considered by the Commission, care should be taken to ensure that they are consistent with other existing requirements. In addition we believe that in order to be effective for consumers, information provisions must be proportionate and focused on key information.

Consistency, however, should not be confused with uniformity. Differences in the underlying structure of products, their tax treatment and capital requirements, will mean that there must also be flexibility within disclosure requirements. For instance, whilst it has been suggested that the same level of disclosure requirements should be applied to unit-linked life products as is applied to UCITS, in our view, the difference between the structures of the these two products make such a direct comparison impossible.

Similarly careful evaluation is needed of any proposal to require advice, taking account of experience in national markets. The level of advice required depends on the complexity of the product in question, and on the circumstances of the consumer. As such flexibility around advice requirements must be an important consideration.

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