



*European Association of Co-operative Banks
Groupement Européen des Banques Coopératives
Europäische Vereinigung der Genossenschaftsbanken*

EACB Response

to EBA Consultation Paper: Draft Guidelines on Product Oversight and Governance Arrangements for Retail Banking Products

10 February 2015

The **European Association of Co-operative Banks** (EACB) is the voice of the co-operative banks in Europe. It represents, promotes and defends the common interests of its 29 member institutions and of co-operative banks in general. Co-operative banks form decentralised networks which are subject to banking as well as co-operative legislation. Democracy, transparency and proximity are the three key characteristics of the co-operative banks' business model. With 3,700 locally operating banks and 71,000 outlets co-operative banks are widely represented throughout the enlarged European Union, playing a major role in the financial and economic system. They have a long tradition in serving 215 million customers, mainly consumers, retailers and communities. The co-operative banks in Europe represent 56 million members and 850,000 employees and have a total average market share of about 20%.

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The voice of 3,700 local and retail banks, 56 million members, 215 million customers

EACB AISBL – Secretariat • Rue de l'Industrie 26-38 • B-1040 Brussels

Tel: (+32 2) 230 11 24 • Fax (+32 2) 230 06 49 • Enterprise 0896.081.149 • lobbying register 4172526951-19

www.eacb.coop • e-mail : secretariat@eacb.coop



Introduction

The European Association of Co-operative Banks (EACB) would like to thank the European Banking Authority (EBA) for the possibility to comment on the proposed guidelines. It has carefully reviewed the consultation document with its members and would like to formulate a number of observations. Some of these are relating to the set of proposed guidelines as a whole ("general comments") and some are answers to the specific questions raised. As the answer form on the website does not allow for general comments, they have been formulated in this document.

General Comments

Even if the EACB and its members share the importance that EBA and its co-supervisors attach to a well developed product oversight and governance process, they nevertheless have serious reservations about the proposed guidelines, as follows:

I. (Legislative) acts or measures already in place

First of all, the EACB would like to stress that there are a number of (legislative) acts/measures already in place or under development at the EU level that intend to cover the various concerns listed in the rationale for the guidelines (e.g. information asymmetry, conduct failure) It concerns:

- The Payment Services Directive (2007)¹ and its revision
- The Consumer Credit Directive (2008)²
- The Capital Requirements Directive IV (2013)³
- The Mortgage Credit Directive (2014)⁴
- The Markets in Financial Instruments II Directive (2014)⁵
- The Payment Accounts Directive (2014)⁶
- The Regulation on Key Information Documents of Investment Products (2014)⁷

As well as:

- EBA Guidelines on Internal Governance 44⁸

Some of these measures have only just been implemented or indeed, still have to be implemented. This being the case, we would consider that it has not been possible to

¹ Directive 2007/64/EC of the European Parliament and of the Council of 13 November 2007 on payment services in the internal market amending Directives 97/7/EC, 2002/65/EC, 2005/60/EC and 2006/48/EC and repealing Directive 97/5/EC

² Directive 2008/48/EC of the European Parliament and of the Council of 23 April 2008 on credit agreements for consumers, 22.5.2008, OJEU L 133/66.

³ Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC, 27.6.2013, OJEU L 176/338

⁴ Directive 2014/17/EU of the European Parliament and of the Council of 4 February 2014 on credit agreements for consumers relating to residential immovable property and amending Directives 2008/48/EC and 2013/36/EU and Regulation (EU) No 1093/2010 Text with EEA relevance, 28.2.2014, OJEU L 60/34-85.

⁵ Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments and amending Directive 2002/92/EC and Directive 2011/61/EU Text with EEA relevance, 12.6.2014, OJEU L 173/349-496.

⁶ Directive 2014/92/EU of the European Parliament and of the Council of 23 July 2014 on the comparability of fees related to payment accounts, payment account switching and access to payment accounts with basic features Text with EEA relevance, 28.8.2014, OJEU L 257/214-246.

⁷ 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)

⁸ EBA Guidelines on Internal Governance, London, 27 September 2011



measure the effect of the various measures on the conduct of financial institutions and their clients in the retail market. Considering at the same time that certain elements of the proposed guidelines are problematic in their implementation and – in general – come with important implementation cost, the EACB would consider the introduction of more and new rules at this point in time pre-mature. Indeed, linking back to the cost-benefit analysis annexed to the Guideline, we would have considered the option to abstain from intervention at this point in time, the best one.

II. Level playing field & ability to (quickly) respond to changing consumer expectations

In addition, we fear that the proposed Guidelines will have a detrimental effect on banks' ability to quickly respond to changing customer expectations, the evolution in product offering as well as the general level playing field between banks and non-regulated entities. Indeed, given that the Guidelines can only regulate "what is already regulated", products/ services not captured by EU texts (yet) are by definition not covered.

The proposed Guidelines introduce a rather heavy-handed administrative regime to the development of new retail banking products. What is more, they seem to steer towards minimization of risks (e.g. Guidelines on Product testing, Product monitoring) where one could argue that a certain degree of risk is inherent to some type of retail banking products. Overall, the burden to introduce a new product becomes significantly higher. As such, we fear that the effect of the guidelines will be that "traditional banks" will have to become more conservative (why introduce a new product when you are not sure it will produce positive results for 100% of the target market with all the compliance consequences and possible litigation costs you may face?). The proposed guidelines would thus make "new" and emerging players benefit even more from their competitive advantage of not being regulated, as they do not face similar process costs nor compliance risks. Indeed, we are concerned that the Guidelines will fail to cover the structures that are not subject to banking supervision today and suggest that exemptions should be considered for supervised credit institutions and their staff to avoid adding to their burden.

III. Proportionality & Subsidiarity

Finally, the EACB is concerned that the proposed guidelines are going beyond what is needed to achieve the intended objective (proportionality) and it is not convinced that there is a need to take action at EU level (subsidiarity).

Proportionality

On the issue of proportionality, there is of course the point made earlier that the effects of legislation in place/about to be put in place have not been measured yet. But in addition to that, there is the following.

Looking at the Guidelines in their current form and the issue they intend to address, also referring back to the ESAs 2013 joint position (see [here](#)) setting out high-level principles on manufacturer's product oversight and governance processes, we learn that the Guidelines intend to address cases of mis-selling based on feedback received by the national supervisory authorities (see annex I, pages 6-7 of the ESA 2013 Joint Position). This NSA-feedback is referring to the sales of more complex investment- insurance and/or mortgage products.



We fail however to understand, how the relatively simple retail banking products that these Guidelines are addressing (comprising for example payment accounts, mass payment products and services and savings accounts) fit into this picture.

In other words: the prescribed processes for product oversight and governance arrangements do not seem proportionate in relation to the relatively simple retail financial products many banks are offering. Instead, they seem to put in place an artificially rigid and heavy governance structure that comes at a considerable cost-without delivering clear benefits.

Subsidiarity

Following the principle of subsidiarity, action at EU level is solely undertaken when proven to be more effective than action undertaken at local, regional or national level. Translating this principle back to current guidelines, we indeed believe that effective action can be and is already undertaken at the national level.

We believe that at the very level of the credit institutions themselves the cumulative impact of: the financial crises, increased levels of transparency and comparability (also because of various EU legislative acts, see also above) and a very competitive market will drive providers to come with the best offer for their customers in times during which it is more than ever necessary to establish a good, all- inclusive and long- term relationship with them. This is all the more true for co-operative banks whose clients are also their members and thus provide for their capital – base.

This being the case, banks themselves have every interest in analysing the impact and consumer-suitability of a potential new product. Taking into account the simple fact that any change in product offering necessitates substantial changes in IT systems as well, no bank would consider introducing a new product without having assured himself of the fact that this product will indeed bring new benefits to the consumer. We therefore see no necessity for a European supervisory authority to prescribe how this should be put in place.

In light of the above points, the EACB would have preferred that EBA, if it really considers the Guidelines as necessary, only applies them to national supervisors and not financial institutions - see an EBA Opinion- rather than the proposed and prescriptive EBA Guidelines, and wonders whether the choice for the latter is justified indeed; unlike ESMA (MiFID II), the EBA does not have a clear and specified mandate for such Guidelines arising from a level 1 text.

Taking into account the fact that both ESMA and EIOPA are undertaking similar efforts, we wish to underline the importance of ensuring for coherence between the different texts- without prejudice to the proportionality approaches that these text hopefully inhibit- so as to ensure for consistency for those credit institutions offering the broad range of services falling within the scope of the aforementioned authorities.

Finally, the EACB considers that the timelines between learning what will be actually the outcome of this consultation (Q2 2015) and having to put the guidelines into practice (April 2016) as very short.

Detailed answers to consultation- questions

- Q2: Do you agree with the delineation of the two sets of requirements for manufacturers and distributors?

Please see our general observations in the enclosed document first.



The distinction between manufacturer and distributor could appear somewhat artificial for those (smaller) institutions that combine both functions in one; an extra layer of bureaucracy is in that case added to their organisation.

Also, the guidelines require a wide communication and cooperation between manufacturers and distributors, which can be difficult to implement especially when they do not belong to the same entity.

For these reasons, we think a distinction should be made in the guidelines between institutions combining both functions and those that are only manufacturer/distributor.

- Q3: Are there any additional requirements that you would suggest adding to either of the two sets of requirements? If so, why?

Please see our general observations in the enclosed document first.

No.

- Q4: Do you agree with Guideline 1 on establishment, proportionality, review and documentation?

Please see our general observations in the enclosed document first.

Although we have fundamental concerns with the Guideline as a whole (see also our general observations in the enclosed document first), we welcome the fact that consideration has been given to the principle of "proportionality" (see Guideline 1.5). . However, we think POG arrangements should be proportionate not only to the nature, scale and complexity of the relevant business of the manufacturer and to the level of complexity of the product **but also to the level of risk associated to the product for the consumer.**

The application of the principle of proportionality should **allow manufacturers and distributors to exclude certain products which are very simple and do not represent a risk for the consumer, from certain or all aspects of the POG arrangements.**

In addition, it is not clear what is meant with "conflicts of interests"; we are not sure that it can be avoided at all times. For this reason, we would like to make the following adjustment to the wording of draft Guideline 1.1

| EBA draft Guideline | EACB proposal | Justification |
|---|---|--|
| 1.1 The manufacturer should establish, implement and review effective product oversight and governance arrangements. The arrangements should be designed to minimise potential consumer detriment , to avoid conflicts of interest, and ensure that the interests, objectives and characteristics of consumers are appropriately taken into | 1.1 The manufacturer should establish, implement and review effective product oversight and governance arrangements. The arrangements should be designed to minimise potential consumer detriment , to minimise avoid conflicts of interest, and ensure that the interests, objectives and characteristics of consumers are appropriately taken into | <i>The meaning of "conflicts of interest" in this context is unclear and we are not sure it can at all times be avoided; the word "minimise" seems therefore more appropriate.</i> |



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- Q5: Do you agree with Guideline 2 on manufacturers' internal control functions?

Please see our general observations in the enclosed document first.

For the reasons outlined in our answer to Question 1, the EACB believes that also Guideline 2 is going beyond –both in nature and in scope- what is necessary to achieve the intended outcome.

We wish to highlight that also in the context of risk management of credit institutions and in the light of corresponding procedures of banking supervision (also following the – national translation of- international Basel III standards), such guidelines have been put in place already.

The guidelines provide that the establishment of the POG arrangements as well as their subsequent review should be endorsed by the management body (2.1). The management body should be the one amending the POG arrangements (2.2).

This systematic endorsement of POG arrangements' reviews implies that the management body has to work in detail on the POG arrangements. Involving the management body in day-to-day management of the institution is not coherent with the its usual level of responsibilities. As written in the GL 44, the management body should instead set and oversee the **overall risk strategy and policy of the institution**.

Since GL 44 provides that the new product approval policy (NPAP) must be approved by the management body, POG arrangements could be endorsed by the management body as a part of the NPAP, but this should not extend to reviews of POG arrangements.

Also, we consider that checking that the staff involved in designing a product is competent and trained on POG issues should be part of the regular Human resources process/training process of the producer. There is no relevant reason to involve directly the senior management.

- Q6: Do you agree with Guideline 3 on the target market?

Please see our general observations in the enclosed document first.

The EACB has two important concerns with Guideline 3 on the target market.

- Firstly, it finds that the Guidelines go too far both in scope and level of prescriptiveness in various ways. As such, it proposes to amend the following:

| EBA draft Guideline | EACB proposal | Justification |
|---|--|---|
| 3.4 The manufacturer should consider how the product fits within the manufacturer's existing product range and whether the presence of too many product variants prevents the consumer from making informed decisions | 3.4 The manufacturer should consider how the product fits within the manufacturer's existing product range and whether the presence of too many product variants prevents the consumer from making informed decisions | <i>It is impossible to objectively assess what is meant with "too many product variants" → what is considered "too much" for one consumer, might be "too little" for the other. In addition, a broader product range would allow manufacturers to phase-in/ phase out certain</i> |



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| | | <i>variants, so as to optimize their product offering.</i> |
| 3.5 The manufacturer should also identify the market segments for which the product is considered likely not to meet their interests, objectives and characteristics and prevent that the product is offered to these market segments | 3.5 The manufacturer should also identify the market segments for which the product is considered likely not to meet their interests, objectives and characteristics and prevent that the product is offered to these market segments | <i>The identification of a "negative target market" seems to go far beyond current practices, especially for (smaller) banks, working with relatively simple products and a very broad definition of "target market".</i> |
| 3.6 When deciding whether a product meets the interests, objectives and characteristics or not of a particular target market, the manufacturer should assess the degree of financial capability of the target market | 3.6 When deciding whether a product meets the interests, objectives and characteristics or not of a particular target market, the manufacturer should assess the degree of financial capability of the target market | <i>We foresee many practical problems when having to assess the degree of "financial capability"⁹ of a given target market. Would the level of education of a consumer be a good indicator and if yes, wouldn't this give rise to discrimination? Are we supposed to "test" consumers on their financial knowledge and keep record? Does experience play a role here, indeed, how does "financial capability" evolve over time?</i> |

- Secondly and on a more fundamental note: the members of EACB design their products with a primary aim to meet the objectives and interests of their clients. As such, they may well identify a "target market" for the products they design. The EACB considers, however, that over-reliance on the notion of "target market" should be avoided, as it is not "exact science". The proposed guidelines risk turning the notion of "target market" - from a marketing/business concept- into a legal term creating compliance risk.

Example of "compliance risk": client A wishes to take out a certain credit product, even though he would not fit into the "target market" that is foreseen for this product. He explicitly asks for the product and, also based on the situation and documentation at hand (client is unemployed but trained to become a surgeon with good prospects on the job market), bank C decides to provide the product to him. After 10 years, the credit product demonstrates poor results at the individual level of client A (also, Client A who in the meantime has a job as a surgeon is divorcing from his wife). Client A sues bank C stating he should never have been provided with the credit product, given that he did not fit into the "target market"

⁹ "Financial capability" here refers to "ability to understand" and not to "ability to (re)pay"



as originally foreseen for this product.

At the same time, a binding definition of “target market” entails the risk, that a client would be systematically cut off from certain products which, in a particular situation, could very well be appropriate/ suitable for him/her (see the same case of Client A above, for whom the credit product delivers good results and who does not divorce from his wife).

The EACB thus considers that the target market identification by the manufacturer should be understood as an indicative guide for those who advise the client and client him/herself, not as a rigid corset from which deviation is possible only on an exceptional and justified basis.

It should be reminded that ultimately, even if we wholeheartedly support the need to provide good information - the choice for a certain product lies with the consumer himself, with the help of - if applicable- the provision of suitable advice.

Moreover, the identification of target market is not relevant for every product included in the scope of the guidelines. Some of these products are adapted to the needs of all consumers. This is the case for example of the payment account. With the adoption of Directive 2014/92/UE creating a right to a payment account associated with basic services, the legislator clearly shows that some products are meeting the interests, objectives and characteristics of all consumers.

Also the Payment Services Directive (2007/64/EC) presupposes that the payment transactions it governs apply to the category consumers in the widest sense- possibly even including micro enterprises (see recital 20 and Article 30(2) of the PSD).

When identifying a target market, the manufacturer should be allowed to create relatively large categories. Having a narrow definition of the target market might require an unjustified intrusion in the privacy of the consumer when trying to determine whether or not he belongs to the target market. It would also be incompatible with some Member States’ national anti-discrimination rules.

- Q7: Do you agree with Guideline 4 on product testing?

Please see our general observations in the enclosed document first.

The issue of product testing at the target market level seems inherently inconsistent. Product testing for a target group with a rather widely defined population and a low degree of granularity would lead to results of little value. To truly take into account the outcome of a stressed scenario, multiple factors should be considered (e.g. in case of a credit contract, one could take into account: level of income, level of education, level of assets, age, family situation and expected developments such as inheritance, birth of children). This would already lead to a description so specific, that it approaches the stress-test of an individual situation.

When the product testing process should lead to assessment and -if applicable- adaptation of products at target market level we fear that this will lead to an overly conservative/ risk avoidant approach in line with the liability issues we see arising from the “target market” concept (see also our responses to Q1 and Q6).

In addition, and as highlighted before: for smaller credit institutions, this procedure seems to introduce unnecessary red tape, considering again the simple nature of the products they often sell.

The product testing for different target-markets would in their case lead to a process that is made artificially complex, without delivering real benefits over and beyond what we



think the set of legislation referred to above (see our general observations in the enclosed document first) will already bring.

Conducting product testing seems not relevant the products included in the scope of these guidelines. It would be of little value to conduct testing for products which are both simple and not risky (deposit account). For other products such as payment cards, for which the risks are associated to fraud and breach of security, it is more important to identify the risks and create appropriate process and solutions than to conduct testing. Indeed, it seems to be more important that consumers receive straightforward information on product features and rights in the context of the selling process, so as to enable them to take informed decisions.

On a positive note, we welcome the fact that the conduct of testing for existing products is limited to the cases where significant changes are made to the product.

- Q8: Do you agree with Guideline 5 on product monitoring?

Please see our general observations in the enclosed document first.

The EACB believes that the Guidelines are not necessary to ensure that credit institutions conduct product monitoring, as it is something that they would want to do in their own interest and something that happens naturally and in various ways:

- At the level of the individual consumer: it is reviewed whether products (still) meet the client's needs
- At a general level: sales- figures can give a good indication of the extent to which products are still "up to date"

In addition, wanting to ensure that a given product continues to meet the interests, objectives and characteristics [of the target market] is already hard at the individual level, where many factors play a role when it comes to changing objectives and characteristics of one's situation; it would seem an impossible task for the target-market level.

- Q10: Do you agree with Guideline 7 on selection of distribution channels?

Please see our general observations in the enclosed document first.

Guideline 7.2 stipulates that the manufacturer should ensure that the products are distributed to the identified target market and only sold outside the target market on a justified and exceptional basis.

We wonder how such distribution [to the target market only] should work in practical terms, in particular when taking the online distribution channels into account.

Furthermore, the combined effect of Guideline 7.2 and 7.3 assumes a level of responsibility on the side of the manufacturer on factors that are beyond its control (i.e. the ultimate distribution of the product); it can be very challenging for a manufacturer to ensure that a distributor acts in compliance with the objective of the manufacturer's POG arrangements, especially in an open distribution model.

- Q12 (on distributors): Do you agree with Guideline 1 on establishment, proportionality, review and documentation?

We welcome the fact that the issue of proportionality is highlighted in Guideline 1.1. We are however –in line with our comments on Guideline 1 having regard to manufacturers-



not entirely clear about what is meant with “conflicts of interest” and therefore we would propose the following amendment:

| EBA draft Guideline | EACB proposal | Justification |
|---|--|--|
| 1.1 The distributor should establish, implement and review effective product oversight and governance arrangements which are specific an proportionate to their size and to their role of bringing products to the market. The arrangements should be designed to minimise potential consumer detriment and to avoid conflicts of interest. | 1.1 The distributor should establish, implement and review effective product oversight and governance arrangements which are specific an proportionate to their size and to their role of bringing products to the market. The arrangements should be designed to minimize potential consumer detriment and to avoid minimise conflicts of interest. | <i>The meaning of “conflicts of interest” in this context is unclear and we are not sure it can at all times be avoided; the word “minimise” seems therefore more appropriate.</i> |

- Q14: Do you agree with Guideline 3 on the knowledge of the target market?

Information provided by manufacturers with regards to target markets should serve as a recommendation only. Ultimately, it is the consumer who should decide whether or not to buy a certain product. Consumers should also have complete freedom regarding the reasons why they decide in favour of certain products.

It is important that consumers receive straightforward information on product features and rights in the context of the selling process which allows them to take informed decisions.

- Q15 (on distributors): Do you agree with Guideline 4 on information?

The level of information to be provided to the “target market” gives rise to a number of questions:

- When the price of the product to be paid by the consumer is to be provided from the outset by the manufacturer and to be disclosed to the consumer by the distributor, no room is left for the distributor to determine its own prices/ fees (i.e. its very business case).
- Also, it is not clear why the distributor should disclose the listed information to the “target market” as a whole, as this could be a wide and undefined group.

| EBA draft Guideline | EACB proposal | Justification |
|---|--|--|
| 4.1 The distributor should take into account disclosures provided by the manufacturer and disclose to the target market a description of the main characteristics of the product; its risks; the total price of the product to be paid by the consumer, including all related fees, charges, and expenses and | 4.1 The distributor should take into account disclosures provided by the manufacturer and disclose to the target market a description of the main characteristics of the product; its risks; the total price of the product to be paid by the consumer, including all related fees, | <i>It is not clear why the distributor should disclose the listed information to the “target market”, as this could be a wide and undefined group. We would have better understood Guideline 4.1 in case it would have required the distributor to disclose the listed</i> |



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| <p>provide additional material supplied by the manufacturer for using the target market. These arrangements are without prejudice to any requirements that may be imposed on distributors through existing and/or forthcoming EU and national legislation on disclosure regimes relating to specific products, or services. Distributors will continue to have to comply with those requirements.</p> | <p>charges, and expenses and provide additional material supplied by the manufacturer for using the target market. These arrangements are without prejudice to any requirements that may be imposed on distributors through existing and/or forthcoming EU and national legislation on disclosure regimes relating to specific products, or services. Distributors will continue to have to comply with those requirements.</p> | <p><i>information to the individual consumer. Should that be the case, however, we wish to highlight that a number of EU legislative acts –some of which only recently entered into force– already foresee in such provisions. Hence, the major part of this guideline seems obsolete.</i></p> |
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As expressed in our concerns with the notion and use of “target market” as per Guideline 3, we see the “target market” notion as an internal “guide”. Not a rigid corset from which deviation is only possible on an exceptional and justified basis.

| EBA draft Guideline | EACB proposal | Justification |
|--|---|---|
| <p>4.1 The distributor should be able to provide information to justify to the manufacturer why they offered a product to a consumer who does not belong to the target market.</p> | <p>4.1 The distributor should be able to provide information to justify to the manufacturer why they offered a product to a consumer who does not belong to the target market.</p> | <p><i>We would thus propose to delete the Guideline for distributors stipulating that the distributor is to provide information to justify to the manufacturer why it has offered a certain product to a consumer who does not belong to the target market.</i></p> |

Contact:

The EACB trusts that its comments will be taken into account.

For further information or questions on this paper, please contact:

- Ms Marieke van Berkel, Head of Department (m.vanberkel@eacb.coop)
- Ms Else Boekesteijn, Adviser, Retail Banking/ Consumer Policy (e.boekesteijn@eacb.coop)