Product oversight for financial institutions

Balanced consideration of customer interests in product development

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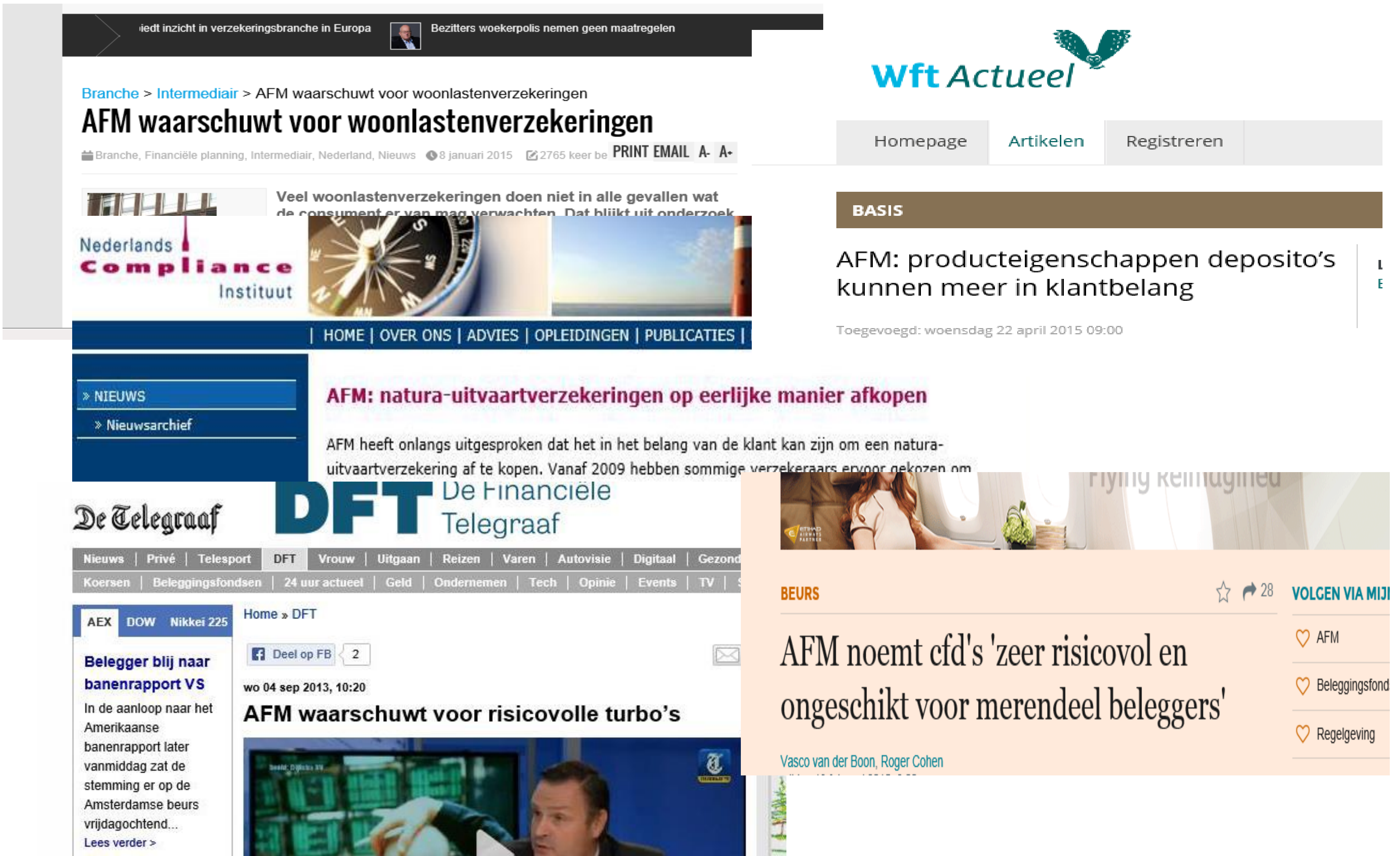
AFM

Autoriteit Financiële Markten

Agenda

1. Introduction
2. Why product oversight?
3. Introduction of legislation
4. AFM’s supervision
5. Evolution since 2013
6. Questions

Introduction



Why product oversight?

1. Consumers were confronted with defect or defunct products

2. Loss of trust in the financial sector

3. Financial stability became an issue due to product scandals

4. Transparency and selling/ distribution rules inadequate

Legislation

1. **On January 1st 2013 legislation was introduced:**

A financial enterprise that offers or structures a financial product and makes such product available shall have appropriate procedures and regulations in place ***to ensure that balanced consideration has been given to the interests of consumers***

The financial product is <u>demonstrably</u> the result of this consideration of interests.

Legislation

*The **target customer** in the financial product has been defined on the basis of an analysis of and description of the target customer's intended objective*

*Tests are conducted in order to establish how such financial product performs as a whole and how the separate elements of such financial product perform under various **scenarios**.*

*The product information and, to the extent that can reasonably be expected, the distribution of the financial product are both **suitable** for the target customer*

*Checks of and, if necessary and appropriate, updates of the procedures and measures shall take place **on a regular basis**.*

Legislation: Limitations

1. Principle based regulations
2. Not all products are under scope (yet!)
3. PARP remains own responsibility
4. Legacy products (unit linked insurance) excluded

Our supervisory approach

Some basic considerations

Responsibility for own product design processes and resulting products: prevent moral hazard

Institutions and products vary: **no one-size-fits-all** approach

Risk-based approach: thousands of products

Conduct of business and **prudential supervision** are related: twin-peaks model

More interested in the way procedures **actually work** in practice than in the way they are documented

Main approach for supervision

The proof is the product

Ask them for their own review of the product

Perform a similar analysis

Discuss both analyses with eachother

Need data

Actuarial data for (life) insurances, probabilities even

Exact costs and characteristics to simulate investment products

Continuous monitoring of product offerings

Thematic or incident driven supervision

Four criteria to determine added value

Value for money

Need

Safety

Complicatedness

Market response and examples

Market reactions: some ‘quotes’

AFM: You do not have the legal powers to supervise the product, but only the process

AFM: I spoke with a consumer who wants this product, and you want to tell me I cannot sell it?

AFM: We have not received any complaints, so who are you to tell us we are not doing it right?

Examples: Products to match expectations

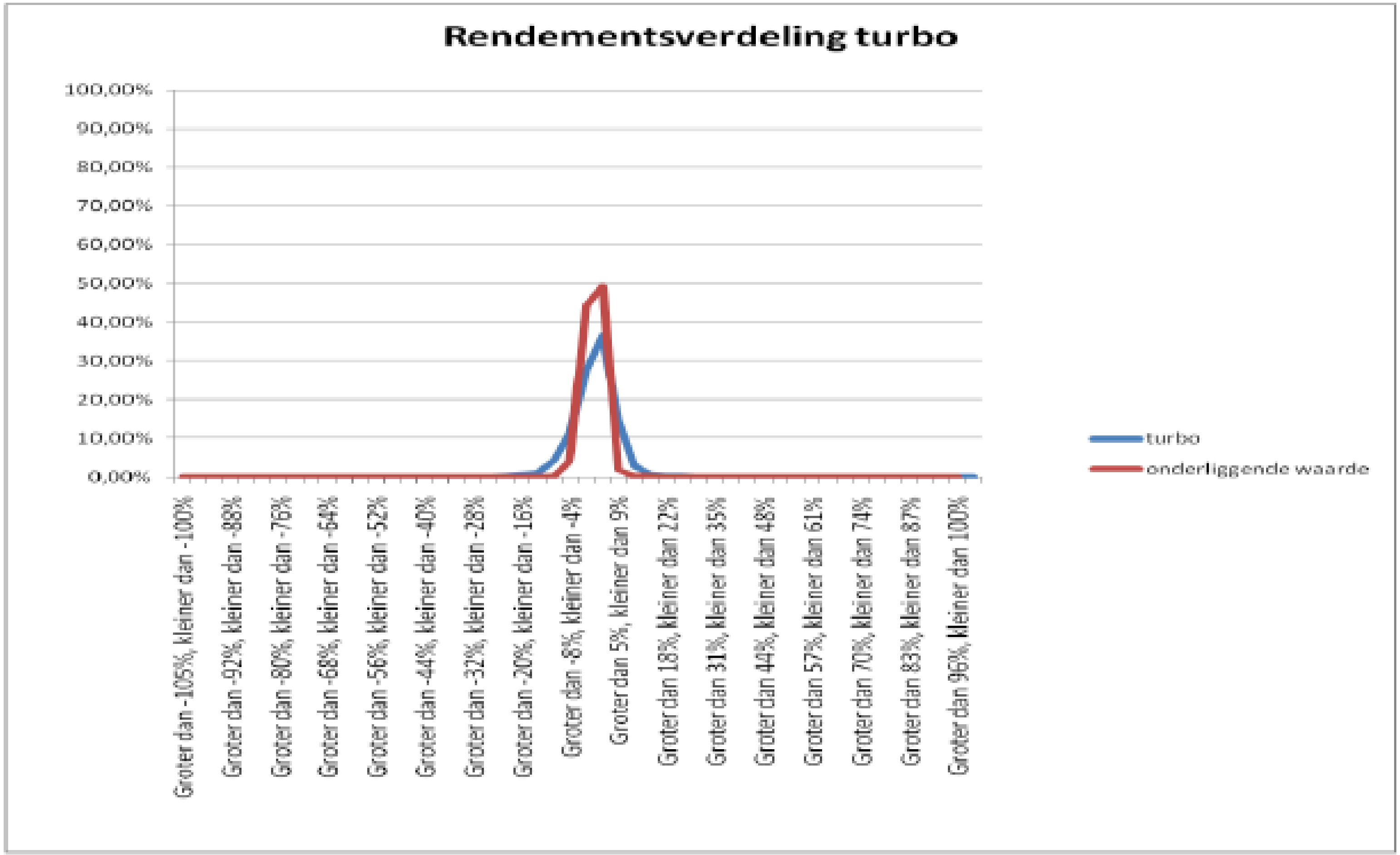
Smart Beta: low volatility ETF

Investment funds

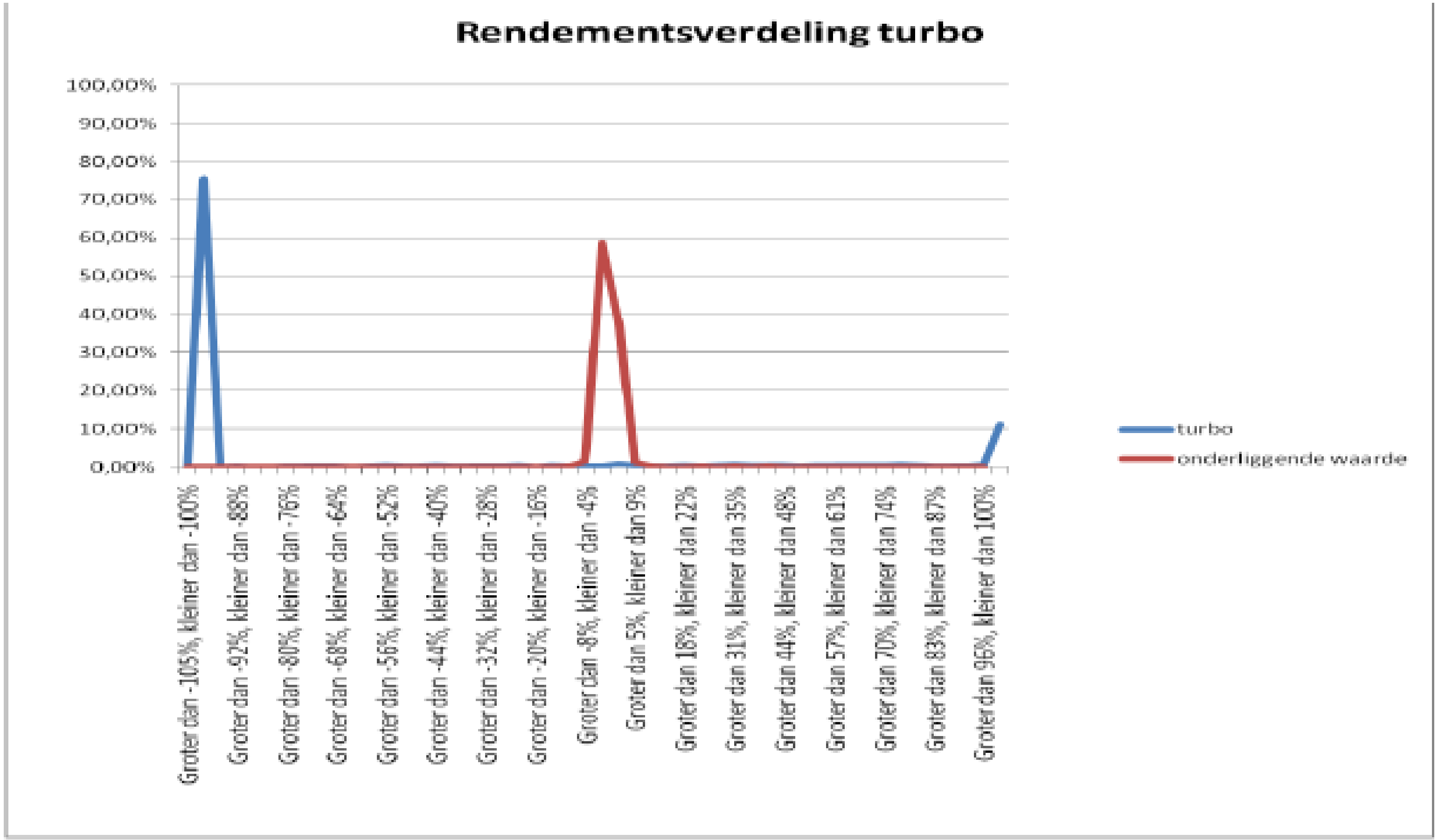
Turbos

Structured products

Turbo Long Gold, leverage 2, holding 5 days



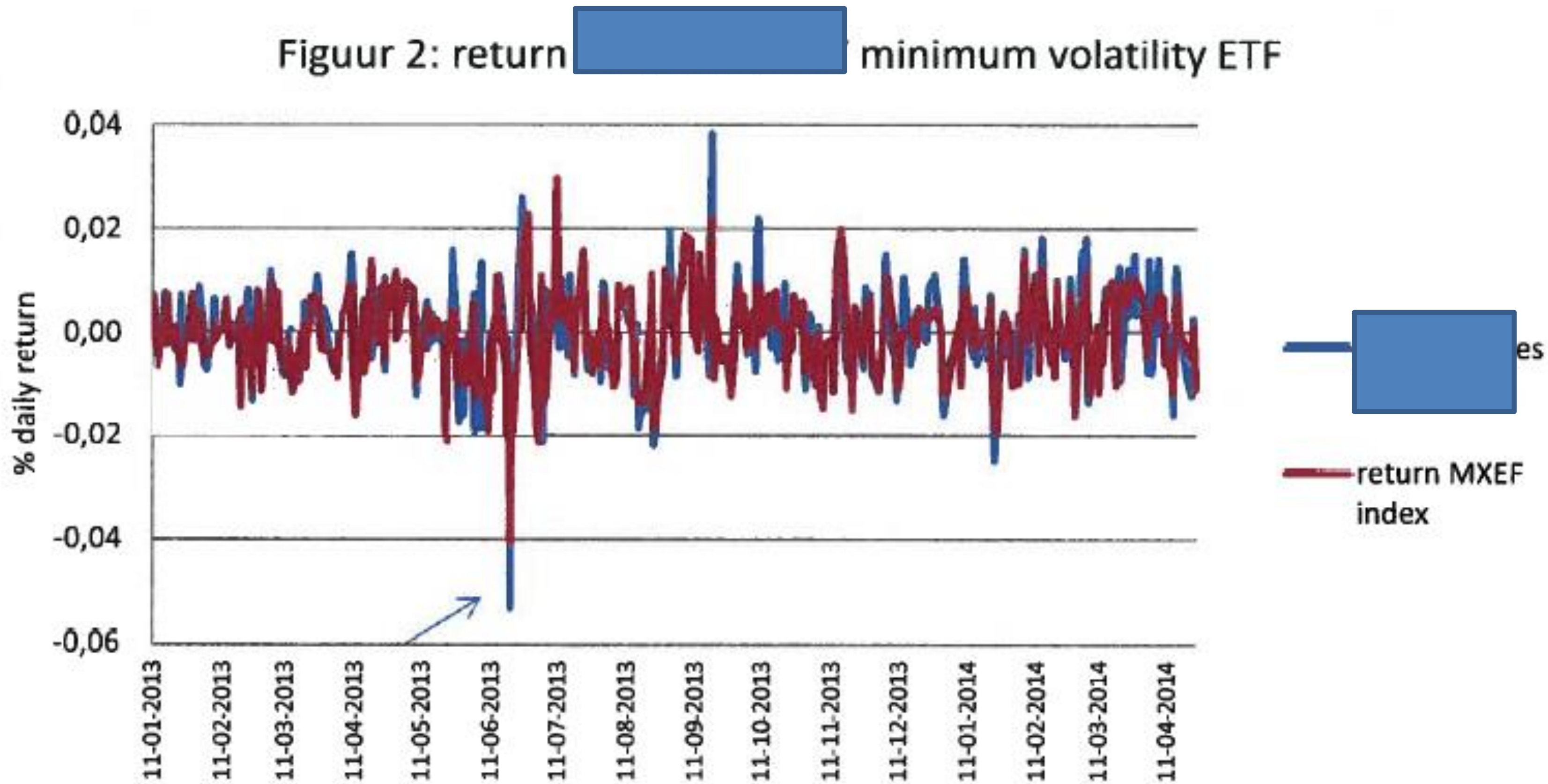
Turbo Short AEX, leverage 195, holding 2 days



Measures taken

- *Nedsipa was founded, to represent all issuers of these products*
- *More and better information, including warnings for high leverage Turbo's*
- *Limitiations were introduced to prevent high leverage Turbo's*

Examples: Products to match expectations



Evolvement of supervision

- *From 2013 on, the focus has mainly been on the product*
- *All investigations showed that a lot of work remains to be done*
- *Focus is shifting, to prevent 'tick the box' exercises*
- *Selfcritical abilities need more 'encouragement'*

Questions?

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