

RETAIL INVESTMENT STRATEGY AND INCENTIVES AND ADVICE REGULATION IN THE INSURANCE DISTRIBUTION DIRECTIVE – CHALLENGES FOR THE FINANCIAL MARKET

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Purpose: The purpose of this article is to analyze the solutions proposed in the RIS amending the provisions of the Insurance Distribution Directive, hereinafter: “IDD” in the field of insurance distribution with an investment element regarding incentives and advice, and to assess their impact on the functioning of the Polish insurance market (OJ EU L 26/19, 2016).

Design/methodology/approach: The article uses the dogmatic-legal method. The article deals with the impact of the Retail Investment Strategy (RIS) on the Insurance Distribution Directive (IDD) regulations. The article defines the concept of incentives and presents the solutions for incentives in the IDD in the current legal state, and then presents the changes proposed in the RIS regarding the IDD. The possible effects of the implementation of the RIS in its current form into the Polish legal system are also identified. The article was written using the dogmatic-legal method.

Findings: The paper indicates the possible effects of implementing RIS in its current form into the Polish legal system. In addition, several legislative proposals for the implementation of RIS into the Polish legal system are presented.

Originality/value: The author is one of the first to present incentive and advisory solutions in IDD and RIS, and then compare them. The article is aimed at researchers, students and practitioners in the financial industry.

Keywords: insurance distribution, inducements.

Category of the paper: Research paper.

1. Introduction

On May 24, 2023, the European Commission published the Retail Investment Strategy (hereinafter “RIS”) (2023/0167 (COD)). RIS amends regulations relating to the distribution of investment products in 5 different areas, i.e. the provision of investment services, the provision of insurance or reinsurance distribution services to third parties, the taking up and pursuit of insurance activities, undertakings for collective investment in transferable securities, and alternative investment fund managers (2023/0167 (COD), p. 5).

According to data published by the European Commission, the EU retail investment market is characterized by a low level of participation by retail investors, with EU citizens largely confined to savings products that generate low returns (2023/0167 (COD), p. 3). In the case of Poland, according to data from the Polish Development Fund on the structure of household financial assets in Q2 2024, the largest item in household financial assets was current settlement deposits (28.3% of assets) (PFR, 2024). In second place were other deposits (12.5%), while cash came in third (11.8%) (PFR, 2024). Together, these three items accounted for 52.6% of household financial assets.

According to the European Commission, RIS aims to change the investment culture, but this is only possible if retail investors gain confidence in the capital markets. In order to increase the confidence of retail investors in the capital markets, RIS implies facilitating access to relevant, comparable and understandable information about an investment product, minimizing the risk of undue influence of unrealistic marketing information, reducing shortcomings in the way products are created and distributed, related to conflicts of interest, and offering value-for-money products to retail investors (2023/0167 (COD), p. 2).

The purpose of this article is to analyze the solutions proposed in the RIS amending the provisions of the Insurance Distribution Directive, hereinafter: “IDD” in the field of insurance distribution with an investment element regarding incentives and advice, and to assess their impact on the functioning of the Polish insurance market (OJ EU L 26/19, 2016). The article uses the dogmatic-legal method.

2. Regulation of incentives in the IDD

In the current state of the law, the concept of incentives appears in Article 2(1)(9) of the IDD, as one of the types of remuneration. The aforementioned article defines remuneration as “any commission, fee, charge or other payment, including an economic benefit of any kind or any other financial or non-financial benefit or incentive, offered or given in connection with insurance distribution activities.”¹ Analyzing the provisions of the IDD, it can be seen that the legislator introduces several mechanisms at the same time to increase customer protection in the insurance market and ensure greater transparency and fairness in the process of selling insurance products.

First, the IDD regulates how insurance distributors themselves are remunerated by other entities such as brokerage houses, as well as how insurance distributors' employees are remunerated and evaluated for their performance. It was pointed out that remuneration and performance appraisal must not be carried out in a way that contradicts the obligation to act in

¹ The current legal status as of 31.01.2025.

accordance with the best interests of their customers. It was stressed that this primarily applies to situations in which an insurance distributor or its employee could have offered a customer a different insurance product that better suited the customer's needs, while it did not do so because the way it was compensated, its sales goals or other issues gave it an incentive to recommend a particular insurance product.

The concept of the best interests of the customer is an example of a general clause, and therefore, in terms of interpretation, refers to a system of extra-legal judgments, i.e. moral, ethical, etc. For this reason, the doctrine points out that it is important to interpret the “best interests” in a specific context, that is, the way the distributor is remunerated - to the prohibition of misselling (sales inadequate to the needs of the customer) (Maśniak, 2020, pp. 104-105).

Depending on the role played in the insurance distribution process, care for the best interests of the customer will be manifested in a different way and should be evaluated through the prism of due diligence required of entrepreneurs, which all insurance distributors are (Maśniak, 2020, pp. 107-108). At the same time, it can be assumed that the introduction of the duty of care for the best interests of the customer equalizes the substantive advantage between the customer and the insurance distributor (Malinowska, 2017, p. 121).

To make it easier to determine which benefits in practice can be considered incentives, the legislature issued a delegated regulation supplementing the IDD with regard to information requirements and business rules applicable to the distribution of insurance investment products.

Article 8 of the delegated regulation indicates the criteria for evaluating incentives, as well as incentive schemes, i.e. the rules under which incentives are paid, such as bonus regulations for insurance agents. Two main criteria for evaluating incentives can be distinguished. First, it is verified whether the incentive may have a detrimental effect on the quality of the relevant service provided to the customer. Second, it is verified whether the said incentive may provide an incentive to act inconsistently with the obligation to act honestly, fairly and professionally in accordance with the best interests of the customer.

In addition to the main criteria mentioned above, there are also specific criteria listed in the delegated regulation. It is worth noting at this point that this is an open catalog, so individual insurance distributors can tighten the criteria for examining incentives or even abandon them altogether. These detailed criteria can be divided into positive criteria, which ensure the return of the incentive paid and refer to qualitative criteria, and negative criteria, which are examples of circumstances in which any form of remuneration or benefit can be considered to have a detrimental effect on the quality of the service provided to the customer (Tarasiuk, 2017, pp. 127-129).

Analyzing the aforementioned specific criteria, it can be concluded that, first of all, insurance distributors should avoid formulating sales targets based only on quantitative criteria, as there is a risk that insurance companies or insurance intermediaries will propose insurance products that are inadequate to meet customer needs in order to achieve an adequate sales volume. The doctrine points out that the mere formulation of sales targets, excess commissions

is not prohibited, but in order not to have a detrimental effect on the interests of the customer, remuneration arrangements for the achievement of certain “sales” targets can be balanced by mechanisms for reducing remuneration in the event of poor quality “sales” (Pokrzywniak, 2018). Another solution currently often used in practice is the combination of quantitative and qualitative criteria, which make the payment of remuneration conditional not only on the achievement of certain quantitative indicators, but also on the maintenance of a low number of customer complaints, a low rate of the percentage of customer cancellations from concluded contracts, due fulfillment of pre-contractual obligations to the customer, etc. (Pokrzywniak, 2018).

Secondly, the legislator introduces the obligation to inform the customer before entering into an insurance contract about the nature of the insurance intermediary's remuneration, including whether he or she receives an economic benefit of any kind offered or provided in connection with the insurance contract². It is worth noting that *expressis verbis* the legislator did not use the phrase incentive, while referring to the definition of incentive, it can be assumed that incentive also falls within the scope of this provision. This provision is supplemented by the obligation to disclose conflicts of interest in the form of an insurance intermediary's ownership of more than 10% of the voting rights or capital in a given insurance company, as well as when an insurance company owns more than 10% of the voting rights or capital of an insurance intermediary³.

In addition, in the case of distribution of an insurance investment product, the customer should be informed of all costs and related fees, including the cost of advice, if such an insurance intermediary provides advice (that is, *de facto* only in the case of an insurance broker), the cost of the insurance investment product itself recommended or sold to the customer, and any third-party payments (Szczepańska, 2015). The insurance distributor should also indicate to the customer precisely the information about the protection part of the remuneration and the investment part, and explain their different function and purpose, in particular, the information should clearly indicate the division of the premium into protection and investment parts (Szczepańska, 2015).

The aforementioned information obligations are intended to enable the customer to make an informed decision regarding the purchase of a particular insurance product. It is worth noting, however, that making an informed purchasing decision requires the customer to have sufficient financial knowledge to be able to draw the right conclusions from the information presented to them. The Eurobarometer survey on financial literacy (financial knowledge and financial behavior were assessed) among EU citizens in 2023 shows that only 18% of EU citizens show a high level of financial knowledge, 64% of EU citizens remain at a medium level, and 18% present a low level of financial knowledge (Flash Eurobarometer, 2025, p. 4).

² Article 19 (1) (d) in conjunction with Article 19(1)(e)(iii) IDD.

³ Article 19 (1) and (2) IDD.

One may, therefore, doubt whether the information obligation is adequately effective to protect the interests of customers. It seems that the legislator himself has acquired doubts about its effectiveness, proposing additional solutions in the RIS to protect the customer from the negative impact of incentives.

Thirdly, the legislator introduces an obligation on the part of the insurance intermediary to study the needs of the customer before offering him insurance, and obliges him to offer the customer a product adequate to his needs⁴. At the same time, it is worth noting that in the case of insurance with an investment element, due to the fact that these products are most often long-term, with high premiums and high sums insured, as well as being a form of pension security, the examination of needs must be more thorough than in the case of other types of insurance.

The legislator explicitly orders the insurance distributor to obtain, prior to concluding an insurance contract, the necessary information regarding the customer's knowledge and experience in the field of investment relevant to the type of product or service, that person's financial situation, including that person's ability to bear losses, his or her investment objectives, and risk appetite, in order to propose an insurance product suitable for him or her, in particular, corresponding to his or her risk tolerance and ability to bear losses⁵.

In the case of the Polish insurance market, in order to make it easier for the insurance intermediary to determine the appropriateness of insurance products for individual customers, the Financial Supervision Commission has issued a recommendation, for insurance companies regarding the product management system (KNF, 2016). According to the recommendation, at the stage of product design, the insurance company should determine the target group of customers to whom the product is to be directed, as well as identify the anti-group, i.e. the group of customers for whom the product will not meet expectations and realize interests (KNF, 10.2, 10.5). With such a division, some customers may not belong, either to the target group for a given insurance product or to the antigroup. Avoiding misselling regarding customers in such a group is the most difficult, and it can be assumed that it involves an individualized analysis of their needs, expectations and interests (Orlicki, 2016, p. 15).

At the same time, it should be noted that a correct analysis of product adequacy is possible when the customer provides complete and true data, and when the insurance intermediary correctly interprets the information obtained from the customer. The doctrine emphasizes that the customer's requirements are the revealed will of the distributor to have insurance coverage for a given subject of insurance and of a certain shape (Orlicki, 2019, p. 3). Resuming, the introduction of the requirement for the insurance distributor to verify the adequacy of the offered contract can be treated as a transfer to the professional entity of a certain element of the decision-making process occurring within the framework of contracting (selection of offers in order to eliminate proposals that are inappropriate in a given situation (Długosz, 2017, p. 133).

⁴ Article 30 IDD.

⁵ Article 30 (1) and (2) IDD.

3. Incentives in RIS

The European Commission considered two ideas for regulating incentives during its legislative work on the RIS (RIS, 2023, p. 10). The first was to ban incentives altogether which would eliminate conflicts of interest arising from the acceptance of incentives by insurance distributors. The second concept was to maintain the current system allowing the payment of incentives under certain conditions while improving and harmonizing incentive disclosure. The second concept was decided upon, but it was assumed that if these solutions did not prove sufficient to protect customers' interests, the Commission would consider extending the ban on incentives.

The first change regarding incentives that the RIS makes to the IDD is a prohibition on accepting or offering incentives for advice provided independently⁶. In order for advice to be considered independent, an advisor must evaluate a sufficiently large number of insurance products available in the market that are sufficiently diverse in terms of type and product providers before making a recommendation⁷. At the same time, such an advisor may not receive any type of remuneration from entities other than the client, such as brokerage houses or insurance companies. The advice of an independent advisor can be limited to well-diversified, non-complex and cost-effective insurance investment products, in order to reduce the time of performance and the price of the service without sacrificing quality for the client⁸. In the case of dependent advice, insurance distributors may accept incentives, provided that the advice is not presented as independent and that the client is informed of the nature and source of the incentives.

The second change is to prohibit the acceptance of incentives in cases where an insurance distributor has not provided individualized advice when offering an insurance product⁹. With that said, incentives in the form of small non-monetary benefits with a total value of less than EUR 100 per year are not covered by the ban. Thus, it can be considered that, for example, advertising gadgets, due to their low value, do not constitute a prohibited incentive.

The third change is the introduction of enumerated requirements that an insurance distributor providing advice should meet in order to consider that advice to a client is provided in accordance with the client's best interests¹⁰. First and foremost, the insurance distributor should analyze a sufficient number of investment products. In addition, the insurance distributor is required to recommend to the client the most cost-effective insurance investment products from those studied and, for comparison, offer at least one financial product without additional features that are not necessary to achieve the client's investment goals and that generate

⁶ Article 2 point 21 RIS.

⁷ Article 2 point 22 d RIS.

⁸ Article 2(20) RIS.

⁹ Article 2 pt. 21 in conjunction with Article 2 pt. 22 RIS.

¹⁰ Article 2 point 21 RIS.

additional costs. This provides the customer with alternative options and, according to his preferences, he can choose the optimal or cheapest product.

At this point, it is worth proposing that during the implementation of the RIS, the legislator consider introducing a statutory minimum number of investment products to ensure that the insurance distributor analyzes a sufficient number of them.

4. Implications of the changes proposed in the RIS for the Polish insurance market

When analyzing the solutions introduced in the RIS regarding incentives in the Polish insurance market, it is necessary to refer to the types of insurance distributors listed in the Act of December 15, 2017, on insurance distribution, which is the implementation of the IDD into the Polish legal system (Journal of Laws 2024, item 1214). An insurance distributor can be an insurance company, as well as insurance intermediaries - an insurance agent and an insurance broker. An insurance agent acts for or on behalf of one or more insurance companies (depending on whether it is an exclusive agent or a multiagent), while an insurance broker represents the customer in seeking insurance coverage and provides a customized recommendation of the best insurance contract.

In view of the prohibition in the RIS on collecting incentives for insurance distributors who do not offer advice, it should be recognized that the prohibition will apply to insurance agents and insurance companies. Only insurance brokers will be allowed to accept incentives if they do not offer independent investment advice. Since insurance with an investment component is currently distributed mainly by insurance agents, the Polish Chamber of Insurers pointed out that in its current form, the implementation of RIS could lead to changes in the market structure, reducing the involvement of agents and insurance companies in offering such products (Bigaj, Durska, Wrzesinski, 2023).

It can also be assumed that due to the ban on the acceptance of incentives by independent advisors, the number of such advisors will decrease, or the prices of such services will increase significantly. This could result in the so-called advisory gap, i.e. a reduction in the availability of investment advice for less affluent clients. There is also a likelihood of a reduction in product offerings to clients due to lower product profitability.

It is also conceivable that the aforementioned restrictions or ban on incentives will create a temptation to introduce new types of fees or increase existing fees, e.g., preparation fee, advisory service fee, portfolio status report fee, portfolio management fee, etc., to make up for the losses caused by the restriction or lack of incentives. This is likely to create the need for more detailed regulations, e.g. in the form of a recommendation from the FSC, to make it more difficult to circumvent the ban.

In this context, during the implementation of the RIS into Polish law, it would be worth considering the introduction of statutory caps on additional fees, which would limit the freedom of insurance distributors in this respect. A similar solution was recently introduced in relation to loans, where the law imposed a maximum on non-interest loan costs.

Presenting the customer with a standard product and the cheapest product may cause customers to be guided in their choices mainly by the criterion of price rather than quality. In addition to a drop in profits for insurance distributors and mutual fund companies, this may cause customers to become disillusioned with the low rate of return on their investments and, consequently, a drop in confidence in the financial market.

In this regard, it is worth advocating for the introduction of financial education programs related to insurance products with an investment component, tailored to different target groups, so that as many clients as possible are able to correctly and independently assess the consequences of their financial decisions.

5. Summary

The idea of the RIS package improving the position of the retail customer is very momentous and necessary in view of the decline in confidence in the financial market. The proposal to introduce a partial ban on incentives seems a good solution, because of the possibility of observing the effects and modifying the system of rewarding insurance distributors adequately to the results obtained. However, due to the possible effects described, it could pose quite a challenge for the financial market. Since the RIS has not yet been enacted in the form mentioned above, changes to its content cannot be ruled out. Once the RIS is enacted, it will then be equally important how the RIS will be implemented into Polish law, which may result in significant changes in the functioning of the Polish insurance market, especially with regard to individualized recommendations (here, in particular, the regulation of the status of an insurance multiagent in terms of the selection of the product offered will be a challenge).

Consequently, before engaging in discussion on the shape of the RIS implementation, it is necessary to reflect on the continued relevance of the multi-agent insurance distributor, which should serve as a starting point for further analysis.

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