Ensuring the Customer's Best Interest in the Polish Insurance Market

Wojciech Paś

1 Introduction

Among the changes introduced by the Insurance Distribution Directive¹ (hereinafter referred to as the Insurance Distribution Directive or the IDD Directive), it is certainly worth noting that Member States of the European Union are obliged to ensure that, when providing the distribution of insurance, insurance distributors always act honestly, fairly and professionally, in accordance with the best interest of their customers. This obligation results from Article 17 (1) of the aforementioned Directive and has been implemented into the Polish legal system in the form of Article 7 (1) of the Act on Insurance Distribution,² which constitutes a reflection of the provision of the Directive in this respect. The main objective of this provision adopted by the European legislator is to try to limit the risk of misselling by insurance distributors, i.e. offering insurance products that are not adequate to the needs and requirements of the specific customer. The sources of misselling distinguished by the European legislator include mainly the remuneration policy of persons responsible for the distribution of insurance products, as indicated in Recital 46 of the Insurance Distribution Directive. According to the European legislator, such a policy should not affect the ability of such persons to act in the best interests of their customers. However, performance-based remuneration itself should not constitute an incentive to offer a particular product to the customer.

The views expressed in this publication are those of the author and do not express the official position of the institution in which he is employed.

¹Directive (EU) 2016/97 of the European Parliament and of the Council of 20 January 2016 on insurance distribution (Official Journal of the European Union, L 26, 2 February 2016).

²Polish Act of 15 December 2017 on Insurance Distribution (i.e. Journal of Laws 2018.2210).

W. Paś (✉)
PZU SA, Warsaw, Poland

The distribution of insurance products under the regime of the Insurance Distribution Directive should be carried out through a test of the customer's requirements and needs based on information received from him or her.³ Any insurance product offered to the customer should always meet his or her requirements and needs. The distribution of adequate insurance products to customers is one of the solutions adopted in the Insurance Distribution Directive, which aims to achieve the fundamental objectives of the Directive, such as increasing the protection of customers in the financial market and restoring their confidence in that market. The Insurance Distribution Directive itself is part of a series of legislative initiatives taken at the European level, designed to increase consumer protection in the insurance market.⁴

In Sect. 2, I interpret the principle of the customer's best interest in light of European and Polish insurance law and Polish supervisory practice, in particular, how this principle is understood in the IDD and MiFID, and what the relationship is between these two legal systems. Next, I analyse the best interest in light of the PFSA's recommendations and the supervisory sanctions which may be applied by the PFSA in the event of a breach of this principle.

The last section is devoted to ensuring the customer's best interest in the Polish insurance market. Within this section, I indicate what actions should be taken to ensuring this principle as well as the impact of the distributor remuneration system on ensuring the application of this principle.

2 The Principle of the Customer's Best Interest in Light of European and Polish Financial Markets Law and Polish Supervisory Practice

2.1 European and Polish Insurance Law

First of all, it should be stated that the principle of acting in the best interest of the customer is a new obligation resulting from insurance law. The previous Insurance Mediation Directive did not impose this obligation on insurance intermediaries.⁵

Ensuring the best interests of the customer is one of the motives of the IDD and appears repeatedly in the provisions thereof.⁶ It is the intention behind many of the obligations imposed on insurance distributors, starting with management and prevention of conflicts of interest by insurance distributors in a manner which ensures that they do not adversely affect the interests of customers, through a system of remuneration of distributors which should not adversely affect their ability to act in

³In accordance with Recital 44 of the Insurance Distribution Directive.

⁴Mrozowska-Bartkiewicz (2016), pp. 112–113.

⁵Directive 2002/92/EC of the European Parliament and of the Council of 9 December 2002 on insurance mediation, Official Journal of the European Union, L 9, 15 January 2003, p. 245.

⁶Malinowska (2018), p. 57.

accordance with the best interests of the customer. It also refers to cross-selling practices which must not lead to a situation where the interests of customers are not properly taken into account.

Article 7 (1) of the Act on Insurance Distribution is the main source of the obligation imposed on insurance distributors to act in the best interest of the customer present in the Polish law. Pursuant to this provision, when distributing insurance policies, an insurance distributor shall act honestly, reliably and professionally, in accordance with the best interests of customers. An insurance distributor within the meaning of the Act on Insurance Distribution is an insurance company, an insurance agent, an agent offering supplementary insurance or an insurance broker.

The development of principle of the customer's best interest is reflected in the requirements relating to the remuneration policy of insurance distributors.⁷ Pursuant to Article 7 (2) of the Act on Insurance Distribution, the method of remunerating insurance distributors and persons with whom the insurance agency activities or insurance brokerage activities are performed, as well as persons with whom the insurance company's distribution activities are performed, may not be contrary to the obligation to act in accordance with the best interests of customers, in particular, an insurance distributor may not make arrangements concerning remuneration, sales targets or other arrangements that could constitute an incentive to propose a specific insurance agreement or insurance guarantee agreement to the customer in a situation where the insurance distributor could propose another agreement that would be better suited to the customer's needs.

Another expression of the principle of the best interest of the customer consists in the requirements relating to the prevention of conflicts of interest by an insurance agent, insurance broker and insurance company in the course of distribution of insurance based-investment products, which are regulated in Article 15 of the Act on Insurance Distribution. In light of this provision, the aforementioned distributors are obliged to make use of organisational solutions aimed at preventing conflicts of interest in such a way that they do not have a negative impact on the interests of customers. Such solutions should be proportional to the business activity conducted and proposed insurance agreements as well as the type of distributor. Within the adopted solutions, distributors referred to in Article 15 of the Act on Insurance Distribution should undertake actions to identify conflicts of interest between them, including their management board members, proxies, employees or other persons related to them, and their customers, or between their customers, arising in the course of conducting business in the distribution of insurance-based investment products. In the event that organisational solutions are not sufficient to avoid the risk of customer detriment, the aforementioned distributors shall, before the conclusion of the insurance contract, disclose the general nature or sources of conflict of interest to the customer, including in particular whether the commission received under the insurance contract depends on the volume of insurance contracts concluded. The information is to be provided on a durable medium and must include appropriate data and

⁷Ziemniak (2019), p. 35 and subsequent.

information taking into account the type of customer and enabling the customer to make an informed decision about the activity of the insurance distributor in relation to which the conflict of interest has arisen.

The principle of the customer's best interest is also subject to the requirements of both Commission Delegated Regulation (EU) 2017/2358 of 21 September 2017 regarding product supervision and management requirements for insurance companies and insurance distributors⁸ and Commission Delegated Regulation (EU) 2017/2359 of 21 September 2017 regarding information requirements and rules of business operations applicable to the distribution of insurance-based investment products.⁹

The requirement for the manufacturer of insurance products to provide all relevant information concerning those products, including information on the product approval process, the specific target market and the suggested distribution strategy, constitutes the implementation of the principle of the customer's best interest under the Regulation with regard to product supervision oversight and governance requirements for insurance companies and insurance distributors. At the same time, manufacturers and distributors of insurance products should take appropriate action when they determine that a product does not correspond or no longer corresponds to the interests, objectives and characteristics of a particular target market. The best interest of customers is also one of the criteria that should be taken into account in the approval process of an insurance product, i.e. at the stage of its development. The main source of obligations related to the principle of the best interest of the customer under the Regulation with respect to information requirements and business rules applicable to the distribution of insurance-based investment products is prevention and management of conflicts of interest and evaluation of incentives as well as incentive schemes under Article 8 of the Regulation.

The principle of acting in the customer's best interest itself can often interact with the existing rules of insurance law in the EU Member States, such as the principle of good faith.¹⁰ Such a situation may mean that the principle of acting in the customer's best interest may *de facto* constitute a repetition of the existing rules of insurance law¹¹ or an emanation of those rules.¹² Irrespective of how it interacts with the existing rules of insurance law, it will also undoubtedly create new obligations for insurance distributors, which may contribute to the harmonisation of legislation in

⁸Commission Delegated Regulation (EU) 2017/2358 of 21 September 2017 supplementing Directive (EU) 2016/97 of the European Parliament and of the Council with regard to product oversight and governance requirements for insurance undertakings and insurance distributors, *OJ L* 26, 2.2.2016, p. 19.

⁹Commission Delegated Regulation (EU) 2017/2359 of 21 September 2017 supplementing Directive (EU) 2016/97 of the European Parliament and of the Council with regard to information requirements and conduct of business rules applicable to the distribution of insurance-based investment products, *OJ L* 145, 30.4.2004, p. 1.

¹⁰Malinowska (2018), p. 64 et seq.

¹¹Marano (2017b), p. 11 and subsequent.

¹²Malinowska (2018), p. 71.

the EU and may also affect the relationship between the supervisory authority and the insurance distributor.¹³ In this context, the principle of acting in the customer's best interest will be a sort of a model of conduct for an insurance distributor in the course of its business and will be subject to assessment by a supervisory institution in accordance with the adopted model.¹⁴ From this perspective, it is desirable and justified for the stability and safety of insurance distributors that supervisory authorities publish their views on their understanding of the principle of acting in the customer's best interest, together with examples of actions which are either consonant with or contrary to this principle.

2.2 *MiFID*

It seems that the provisions of Directive 2004/39/EC on markets in financial instruments (MiFID Directive)¹⁵ and Directive 2014/65/EU on markets in financial instruments¹⁶ could have been the reference point for the adoption of obligations related to acting in the best interest of the customer for insurance distributors, as could be indicated by Recital 10 of the IDD Directive, which states the need to ensure effective consumer protection in all financial sectors and the need to ensure the harmonisation of regulations. The concept of acting in the best interest of the customer adopted in the IDD Directive reflects the obligations imposed under the MiFID Directive. Pursuant to Article 19 of the MiFID Directive, Member States require that, when providing investment services and/or, where appropriate, additional services to customers, an investment company shall act honestly, fairly and professionally in accordance with the best interests of customers. The aforementioned provision is the source of the obligations associated with investment companies acting in the best interests of their customers.

The MiFID requirements for acting in the best interests of the customer focus primarily on customer information obligations in relation to the investment company providing the services, the financial instruments and the proposed investment strategies, which should include appropriate guidance and warnings about the risk associated with investment in such instruments or in relation to particular investment strategies, as well as information about the executors, costs and related fees. The aforementioned information should be structured in such a way that the customers or potential customers are able to understand the nature and risks of the investment

¹³Malinowska (2018), p. 11 et seq.

¹⁴Malinowska (2018), p. 11 et seq.

¹⁵Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments (amending Council Directives 85/611/EEC and 93/6/EEC and Directive 2000/12/EC of the European Parliament and of the Council and repealing Council Directive 93/22/EEC)—(MiFID).

¹⁶Directive 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.

service and the specific type of financial instrument offered and thus to make informed investment decisions. Another area related to acting in the best interest of the customer is the obligation to examine the knowledge and experience of the customer in the field of investment relevant to the specific type of product or service, his/her financial situation and investment objectives in order to allow the investment company to determine whether the proposed investment service and financial instrument are appropriate for the customer. At the same time, when an investment company concludes that a product or service is not appropriate for the customer or potential customer, it must advise the customer of that fact. A similar obligation is imposed on the investment company in the event that the customer refuses to provide information about his/her knowledge and experience or if this information is insufficient for assessing suitability; in such a case the investment company is required to warn the customer that it is unable to assess the suitability of a particular product or service.

The principle of the customer's best interest is also the core of the MiFID II¹⁷ system of regulations, including in particular Directive 2014/65/EU on markets in financial instruments, which expands the scope of obligations related to this principle.¹⁸ In particular, in accordance with Recital 71 of Directive 2014/65/EU, investment companies should therefore understand the characteristics of the financial instruments they offer or recommend and develop effective strategies and arrangements to identify and review the categories of customers to whom products are to be delivered and services are to be provided. Member States should ensure that investment companies creating financial instruments guarantee that those products are developed in order to satisfy the specific needs of the target market, i.e. end-customers, within a specific customer category, that they take reasonable steps to ensure that financial instruments are distributed within a specific target market, and that they periodically review the target market identification data and the performance of the products offered. Investment companies offering or recommending financial instruments which are not products developed by them should also have adequate arrangements in place to obtain and understand relevant information regarding the product approval process, including the specific target market and the characteristics of the product they are offering or recommending. Such an obligation should apply without prejudice to any adequacy or suitability assessment to be carried out subsequently by the investment company in the course of providing investment services to each customer based on his or her personal needs, characteristics and objectives.

The overriding objective of the obligation to act in the customer's best interest is to protect investors from misconduct, which is not safeguarded by other more specific MiFID II requirements.¹⁹ Thus, a breach of the general requirement related to the obligation to act in the best interests of the customer does not necessarily

¹⁷Malinowska (2018), p. 59.

¹⁸Malinowska (2018), p. 59.

¹⁹Della Negra (2019), p. 34 and subsequent.

involve a breach of more specific requirements. The purpose of the duty to act in the customer's best interest is to safeguard the interests of the client in a comprehensive manner, which is not may be guaranteed by more specific requirements.²⁰

Preventing asymmetry of information between a professional such as an investment firm or intermediary firms and a client is also identified as one of the objectives of the rules regarding the conduct of business in MiFID II.²¹

Under MiFID II, the customer's best interest is perceived through the implementation of the requirements set out in Articles 24–25 of MiFID II, consisting primarily in the assessment of the suitability and adequacy of instruments and reporting to clients.²² Moreover, the principle of acting in the best interests of its clients under MiFID II is also implemented by the product governance requirements.²³

2.3 *MiFID vs. IDD*

Undoubtedly, the MiFID regulations have influenced the shape of European insurance law, as can be seen in Recital 10 of the IDD, which states that there is a need to ensure effective consumer protection in all financial sectors and to ensure the harmonisation of rules. This phenomenon has been described in publications as “Mifidization” of European insurance law and is manifested by its impact on: (a) the sources of insurance law, (b) the insurance product management system, (c) customer protection, (d) interpretations of the rules on life insurance by the EU national courts.²⁴

The adoption of similar legal solutions for MiFID-regulated investment products and IDD-regulated insurance-based investment products is intended to prevent regulatory arbitrage and thus to avoid encouraging the creation of financial products that are not subject to a more stringent legal regime.²⁵

The best example of the impact of the MiFID on European insurance law is the Commission Delegated Regulation (EU) 2017/2358 of 21 September 2017 with regard to product oversight and governance requirements for insurance undertakings and insurance distributors, which reflects the legal framework adopted under the MiFID.²⁶

This includes in particular requirements relating to the management of insurance products for manufacturers and distributors of insurance products, such as the obligation to construct a relevant target market and a relevant “antigroup”, i.e. the

²⁰Della Negra (2019), p. 34 and subsequent.

²¹Della Negra (2019), p. 27 et seq.

²²Gortsos (2018), p. 68 and subsequent.

²³Gortsos (2018), p. 71 et seq.

²⁴Marano (2017a), p. 219 et seq.

²⁵Marano (2017a), p. 221 et seq.

²⁶Marano (2017a), p. 222 et seq.

customer group for which the insurance product will generally not be suitable given their needs, characteristics and objectives.

Although similar legal solutions have been adopted in both the MiFID and the IDD, there are also some differences between these legal systems (e.g. a regulation concerning incentives) which may contribute to the creation of a regulatory arbitrage within this framework.²⁷ It is also significant that the MiFID II system is based on the maximum harmonisation of EU law within the legal orders of the Member States, as opposed to the IDD system, which is based on minimum harmonisation of the law, which means that EU Member States may introduce more restrictive regulations.²⁸ Examples of such legal solutions adopted in selected EU Member States which increase the requirements for insurance distributors compared to the IDD regulation were presented in the EIOPA report—*Report analysing national General Good rules in the context of the proper functioning of the Insurance Distribution Directive (IDD) and the internal market*.²⁹

The objectives of both legal systems, i.e. the IDD and the MiFID, are generally complementary. Their core is to provide greater protection for recipients of financial products. Nevertheless, it should be agreed that the creation of regulations for financial institutions should take into account the specific nature of the products they create.³⁰ The nature of insurance products is different from that of other products related strictly to investment. Therefore, similar legal solutions in the financial market should be adopted while taking into account the specificity of a particular business sector.

2.4 Polish Supervisory Practices on the Insurance Market

Although the obligation to act in the best interest of the customer did not exist until the Act on Insurance Distribution came into force in Polish insurance law, the obligation to act as an insurance intermediary taking the best interest of the customer into account was already included in the recommendations of the Polish Financial Supervision Authority (PFSA) for insurance companies concerning their product management systems, in force since 1 July 2016. At this point, it should be noted that the PFSA's recommendations are not universally binding provisions of law, and constitute solely an expression of supervisory expectations addressed to insurance or reinsurance companies with respect to their operations. In this sense, a supervisory recommendation is an indication of what approaches by an insurance or reinsurance company are approved by the supervision authority and therefore not questioned by

²⁷Kern (2018), p. 31; Noussia and Siri (2019), p. 42 and subsequent.

²⁸Kern (2018), p. 31 et seq.

²⁹<https://eiopa.europa.eu/Pages/News/EIOPA-examines-national-general-good-rules.aspx>.

³⁰Cousy (2017), p. 48 et seq.

the PFSA.³¹ As a consequence, recommendations constitute an expression of how the PFSA perceives certain areas of an insurance company's activity, and actions by the supervised entity to the contrary may, in situations specified in legal regulations, result in the initiation of supervisory proceedings.³² However, it should be emphasised that the simple non-compliance of an insurance company with a recommendation cannot constitute the basis for imposing supervisory sanctions by the PFSA. Violation of the applicable provisions of law is a circumstance that constitutes the basis for the application of supervisory instruments by the PFSA. However, it is possible that a specific recommendation will adopt the content of a legal standard.³³

2.5 Responsibility Linked to the Principle of the Customer's Best Interest in the Polish Legal System

The above may have a special significance in the context of the insurance companies' implementation of the requirements resulting from the Act on Insurance Distribution, including the obligation to act in accordance with the customer's best interest. This is because the authority responsible for supervision of the performance of actions taken in the area of insurance and reinsurance distribution is the Polish Financial Supervision Authority, which is entitled to apply supervisory sanctions in the event of the distributors' failure to fulfil certain obligations. One of the bases for the PFSA to apply supervisory sanctions referred to in Article 84 (1) of the Act on Insurance Distribution is the distributors' violation of the obligation to act in the best interest of the customer, i.e. violation of the rule specified in Article 7 (1) of the Act on Insurance Distribution.³⁴

³¹Wojno (2017a).

³²Wojno (2017a).

³³Wojno (2017a).

³⁴In this situation, the PFSA may choose from among the following administrative decisions:

1. issue a public statement indicating the person responsible for the violation and the nature of the violation;
2. order the insurance or reinsurance distributor to cease the violation and refrain from repeating it;
3. suspend a member of the management board of an insurance or reinsurance distributor who is a legal person and is responsible for the violation for a period not exceeding 6 months;
4. impose a fine on an insurance or reinsurance distributor who is a legal person, not exceeding the amount of PLN 21,827,500 or 5% of annual net revenues on the sale of goods and services and financial operations or—in the event of an insurance or reinsurance company—5% of the gross premium written, disclosed in the last financial statements for the financial year, approved by the approval authority of the insurance or reinsurance distributor, or twice the amount of benefits obtained or losses avoided as a result of the violation, if these can be determined;
5. impose a fine on an insurance or reinsurance distributor who is a natural person, not exceeding the amount of PLN 3,055,850 or twice the amount of benefits obtained or losses avoided as a result of the violation, if these can be determined;

Applying the sanction referred to above may be preceded by the issuance of a recommendation by the PFSA against a distributor committing a violation under Article 84 (3) of the Act on Insurance Distribution. The application of supervisory measures by the PFSA is this authority's prerogative, but not its obligation.³⁵ Nevertheless, the supervisory authority's obligation under Article 85 of the Act on Insurance Distribution is to take into account significant circumstances related to the breach when selecting the type and amount of the supervisory measure.³⁶

Notwithstanding the above, it is also worth mentioning the consequences under civil law of the non-adaptation of an insurance product by the distributor to the demands and needs of a customer, which may take different forms depending on the situation.³⁷

2.6 *Best Interest in Light of the PFSA's Recommendations*

Referring to the obligation to act as an insurance intermediary, and taking into account the best interest of the customer referred to in the PFSA recommendations concerning the product management system, it should be pointed out that, in accordance with Recommendation No. 19.2, *In the case of an intermediary for whom the amount of commission depends exclusively on the level of sales, the Company should ensure and demonstrate that the manner of determining the commission does not interfere with the intermediary's obligation to act in the best interest of the customer.* These recommendations also refer to other obligations of the insurance company, which may be perceived as the elements of acting in the best interest of the customer. This applies especially to the obligation to distribute the specific insurance products to a specific target market and to identify an "antigroup", i.e. a group of customers for whom the product will not be adequate. In the preamble

6. withdraw the authorisation to conduct brokerage activity from an entity performing such activity, who violates the law, or remove an insurance agent or an agent offering supplementary insurance, who violates the law, from the register of insurance agents.

³⁵Wojno (2017b).

³⁶These circumstances include:

1. the gravity and duration of the violation;
2. the degree of responsibility of the insurance distributor or reinsurance distributor;
3. the financial situation of the insurance distributor or reinsurance distributor;
4. the amount of benefits obtained or the amount of losses avoided—when these can be determined;
5. the amount of losses incurred by customers and other persons in connection with the infringement—in the case when these can be determined;
6. the insurance or reinsurance distributor's willingness to cooperate with the supervisory authority;
7. the measures taken by the insurance or reinsurance distributor to prevent a repeated violation of the law;
8. the previous violations committed by the particular insurance or reinsurance distributor.

³⁷See more in Kucharski (2019).

to the aforementioned recommendation, which constitutes a kind of statement of reasons for its issuance, the supervisory authority first of all pointed to the need to ensure an effective product management system covering the full product life cycle, i.e. from the moment of its design to the moment of its withdrawal from the market and fulfilment of contractual obligations by the insurance company, which have an impact not only on the financial results and solvency of the insurance company, but also on the quality of the insurance company's relations with its customers. It seems that the last element may have been crucial for the PFSA's need to issue the recommendations in question, taking into account the scale of missellings in the distribution of insurance products³⁸ in recent years as well as in the context of the related risk for insurers. As the PFSA points out in the preamble to the recommendation, the quality of the product management system affects many important areas in the activity of insurance companies and may involve many different types of risks. The PFSA's recommendations are meant to indicate supervisory expectations concerning prudent and stable product management, including the risks associated with this process. In the context of the above, it is also worth mentioning the PFSA's parallel recommendations for insurance companies concerning product adequacy, which refer to the company's obligation to offer insurance customers investment products that meet both the needs and capabilities of those customers (in accordance with Recommendation No. 8). This should be preceded by an examination of the customer's knowledge, experience in the field of life insurance and his or her financial situation. According to the PFSA, these recommendations aim to increase the level of customer protection in the area of insurance-based investment products by ensuring an appropriate information policy towards them and to match them to their needs and capacities.

The need for insurance companies and insurance intermediaries creating an insurance product to identify the target market and the "antigroup" is also clearly highlighted in the EIOPA's preliminary guidelines on product oversight and governance arrangements by insurance undertakings and insurance distributors, published on 13 April 2016.³⁹ In light of the preamble to the EIOPA guidelines, product supervision and management arrangements play a key role in customer protection and are intended to limit the risk of misselling by, *inter alia*, distributing insurance products to the target market. At the same time, the European supervisory body points out that they constitute a key element of the regulatory requirements of the Insurance Distribution Directive. It is important to underline that the EIOPA guidelines are preliminary in nature. Nevertheless, it should be noted that Poland has declared its willingness to comply with the guidelines through the PFSA

³⁸Orlicki (2016), p. 4.

³⁹Preparatory Guidelines on product oversight and governance arrangements by insurance undertakings and insurance distributors. <https://eiopa.europa.eu/Pages/Guidelines/Preparatory-Guidelines-on-product-oversight-and-governance-arrangements-by-insurance-undertakings-and-insurance-distributor.aspx>.

recommendations concerning the product management system and recommendations concerning product adequacy testing.⁴⁰

3 Ensuring the Customer's Best Interest in the Polish Insurance Market

The obligation on the insurance distributor to act in the best interest of the customer, as laid down in the IDD and subsequently reflected in the Act on Insurance Distribution, is not an entirely new obligation for insurance companies. This obligation, although it had not been present previously in insurance law, had been reflected in the recommendations of the Polish Financial Supervision Authority for insurance companies relating to the product management system and product adequacy testing, which have been in force since 1 July 2016. The PFSA's recommendations were certainly inspired by the MiFID regulations, as well as the proposed EIOPA preliminary guidelines on product oversight and governance arrangements by insurance undertakings and insurance distributors and IDD regulations. The introduction of new requirements for insurance companies was caused by irregularities in the Polish insurance market in the area of distribution of insurance-based investment products. The main source of these irregularities was mis-selling.⁴¹

This may be significant in the context of meeting the insurance distributors' obligation to act in the best interest of the customer. One of the intentions behind the adoption of the aforementioned recommendation by the PFSA was to improve the relations of customers with insurance companies, and in particular to prevent the risk of mis-selling and ensure the usefulness of insurance for policyholders and the insured.⁴² These values also seem to have guided the European legislator, as can be seen in particular Recitals of the IDD. In this context, the realisation of the customer's best interest in the course of insurance distribution should be seen as ensuring the adequacy of the product to the customer's needs and requirements. In this sense, an insurance product offered to a customer should meet his or her needs and requirements for the desired insurance coverage. It seems that the intensity of efforts to ensure the customer's best interest should depend on the type of distributor offering a particular insurance product to the customer.⁴³ This is because the role of an insurance agent is different from that of an insurance broker.

⁴⁰Preparatory Guidelines on product oversight and governance arrangements by insurance undertakings and insurance distributors. <https://eiopa.europa.eu/Pages/Guidelines/Preparatory-Guidelines-on-product-oversight-and-governance-arrangements-by-insurance-undertakings-and-insurance-distributor.aspx>.

⁴¹Communication from the Polish Financial Supervision Authority regarding the issued recommendations: https://www.knf.gov.pl/o_nas/komunikaty?articleId=54879&p_id=18.

⁴²Orlicki (2016), p. 9.

⁴³Also in: Malinowska (2017), pp. 120–121; Orlicki (2017), p. 24.

Acting in accordance with the best interest of the customer is interpreted by Polish legal doctrine as such a course of action that is “fair, honest, with regard to the highest level of reliable and exhaustive information and with regard to the customer’s needs, on the basis of a professional analysis carried out in accordance with Article 8 (1) of the Act on Insurance Distribution”.⁴⁴ This procedure should be characterised by the fulfilment of all the obligations resulting from the Act on Insurance Distribution, and its effect should be to propose an optimal insurance contract (i.e. one which is adequate to the needs and requirements of the customer), taking into account the type of distributor.⁴⁵ The duty to act in the customer best interest of the client is a guarantee to safeguard her/his rights in situations when this is not guaranteed by more specific duties.

3.1 Actions Aimed at Ensuring the Customer’s Best Interests

The first step towards ensuring the customer’s best interest, appropriate for each type of distributor, is first of all be to determine the needs and requirements of the customer in order to identify an adequate insurance product. Establishing the needs and requirements of the customer would seem to be an indispensable element for acting in his or her best interest.⁴⁶ The lack of knowledge of the customer’s expectations regarding the desired insurance coverage makes it impossible for the distributor to offer an insurance product meeting his or her needs. Moreover, the obligation of the insurance distributor to determine the customer’s requirements and needs prior to conclusion of the insurance contract on the basis of the information obtained from the customer is laid down in Article 8 (1) of the Act on Insurance Distribution. In accordance with that provision, *before an insurance contract or an insurance guarantee contract is concluded, the insurance distributor must, on the basis of the information received from the customer, identify his requirements and needs and provide objective information on the insurance product in an intelligible form in order to enable the customer to make an informed decision.* The aim of the analysis of the customer’s needs and expectations should be to identify the subject of the coverage and the risks the customer wants to insure against.⁴⁷

Another element common to each type of distributor, the objective of which is ensuring the best interest of the customer, is to ensure compliance of the proposed insurance agreement with the needs and expectations of the customer in terms of insurance coverage, which has been specified in Article 8 (3) of the Act on Insurance Distribution. Nevertheless, it seems that the implementation of this obligation should take into account the specificity of each distributor. Compliance with this obligation

⁴⁴See Nowak (2018), p. 72 et seq.

⁴⁵Ziemniak (2019), p. 38.

⁴⁶See more: Pokrzywniak (2018), p. 71 et seq.

⁴⁷See Tarasiuk and Wojno (2018), p. 7.

by an insurance agent acting in the name and on behalf of an insurance company and an insurance broker acting in the name and on behalf of a customer should be assessed differently. The specificities of the different distribution channels are also recognised by the European legislator who, in Recital 17 of the IDD, states that *this Directive should take into account the differences in the types of distribution channel. It should, for example, take into account the characteristics of insurance intermediaries who are under a contractual obligation to conduct insurance distribution business exclusively with one or more insurance undertakings (tied insurance intermediaries) which exist in certain Member States' markets, and should establish appropriate and proportionate conditions applicable to the different types of distribution.*("...").

In this context, it should be stated that assessment of the fulfilment of the obligation to act in the best interests of the customer should be seen from the perspective of the distributor type. The role of an insurance broker should be to ensure that the maximum conditions of insurance coverage for its customer are provided. Other distributors, including insurance agents, who act in the name and on behalf of the insurance company should pursue the best interests of the customer by ensuring that the product is adequate to the customer's needs and capacities, in particular by ensuring the usefulness of the insurance product for the customer.⁴⁸ At this point it should be emphasised that the obligation to act in the best interest of the customer applies to all actions performed by an insurance distributor in the course of insurance distribution.

3.2 Distributor's Remuneration and the Customer's Best Interests

In my opinion, one main factor that may affect the activity of an insurance distributor in accordance with the best interest of the customer is how the distributor is remunerated. This has also been recognised by the European legislator as indicated in Recital 46 of the IDD. According to the European legislator, such a policy should not affect their ability to act in the best interests of their customers. However, performance-based remuneration itself should not constitute an incentive to offer a particular product to the customer. This principle has been reflected in the provisions of the IDD Directive and the Act on Insurance Distribution. Pursuant to Article 7 (2) of the Act on Insurance Distribution, *the method of remunerating insurance distributors and persons with whom the insurance agency activities or insurance brokerage activities are performed, as well as persons with whom the insurance company's distribution activities are performed, may not be contrary to the obligation to act in accordance with the best interests of customers, in particular, an insurance distributor may not make arrangements concerning remuneration,*

⁴⁸Orlicki (2016), p. 9; Paś (2018), p. 57.

sales targets or other arrangements that could constitute an incentive to propose a specific insurance agreement or insurance guarantee agreement to the customer in a situation where the insurance distributor could propose another agreement that would be better suited to the customer's needs. This requirement is already present in the PFSA's product management system recommendations. On the basis of Recommendation No. 19.2, the insurance company should ensure and demonstrate that the manner of determining the commission does not interfere with the intermediary's obligation to act, with consideration of the customer's best interest.

In light of the above, the rules relating to the remuneration of insurance distributors should be designed in such a way that they do not encourage misselling and thus are not contrary to the duty to act in the best interests of the customer.⁴⁹ The above should be perceived in terms of ensuring that the insurance product is adequate to the customer's needs and capacities. Thus, it seems unacceptable to construct remuneration rules that will motivate insurance distributors to distribute insurance products which do not meet the needs of their customers. However, it should be noted that insurance-based investment products are additionally subject to specific requirements set out especially by Commission Delegated Regulation (EU) 2017/2359 of 21 September 2017 regarding information requirements and rules of business operations applicable to the distribution of insurance-based investment products.

3.3 Ensuring the Best Interest of the Customer as a Way to Limit Misselling

The distributors' implementation of the principle of the best interest of the customer should be seen as an imperative to deal with customers in a way that does not result in the distribution of insurance products which are not adequate to the needs and expectations of customers. In this context, the fulfilment of the obligation to act in the best interest of the customer could be treated as compliance with the prohibition of practices infringing on the collective interests of customers in the form of misselling in financial services, laid down in the Polish legal system in Article 24 (1) in conjunction with Article 24 (2)(4) of the Act on Competition and Consumer Protection.⁵⁰ In light of those provisions, it is prohibited *to propose to customers that they purchase financial services which do not meet their needs as determined with regard to the information available to the trader concerning the characteristics of those customers or to propose to them that they purchase those services in a manner which does not correspond to their nature.* The explanatory memorandum to the inclusion of financial service misselling in the catalogue of

⁴⁹Ziemniak (2019), p. 35 et seq.

⁵⁰Ustawa z dnia 16 lutego 2007 r. o ochronie konkurencji i konsumentów (Act of 16 February 2007 on competition and consumer protection) (uniform text: Journal of Laws of 2017, item 229).

practices affecting collective customer interests explains the prohibition of inadequate financial services as follows: “The planned regulation, introducing a ban on offering financial services that do not meet the needs the consumers they are offered to, determined with regard to the information available to the trader about the characteristics of these consumers or proposing they purchase these services in a manner that does not correspond to their nature, is aimed at forcing traders to behave ethically when offering financial products to consumers. They must assess their products in terms of their suitability for certain groups of consumers and direct them to the groups for which the product is actually intended, in a manner which is not misleading and in conformity with the accepted principles of morality”.⁵¹ Consequently, it can be concluded that proper implementation of the best interests of the customer will certainly reduce the risk of breaching the ban on the misselling of financial services, including in the area of insurance distribution.⁵²

4 Conclusion

The obligation to act in accordance with the best interests of the customer is not a new obligation for the participants in the Polish insurance market. It has already been reflected in the PFSA’s recommendations concerning product management systems. This obligation should be qualified as an imperative to deal with customers in a manner that does not result in the distribution of insurance products which are not adequate to the needs and expectations of customers. Proper implementation of the best interest of the customer will certainly reduce the risk of violating the ban on misselling of financial services. It seems that the intensity of efforts to ensure the customer’s best interest should depend on the type of distributor offering a particular insurance product to the customer. The fulfilment of this obligation by insurance distributors should be assessed from the perspective of ensuring that the product is adequate to the needs and expectations of the customer, in particular guaranteeing that the insurance is useful for the customer, which means that it is adequate to his/her needs and capacities to cover his/her expected insurance cover. The duty to act in the customer’s best interest is a guarantee to safeguard her or his rights in situations when this is not guaranteed by more specific duties.

⁵¹ Wędrychowska-Karpińska and Wiercińska-Krużewska (2016).

⁵² Orlicka (2015), p. 48.

References

- Cousy H (2017) Changing insurance contract law: an age-old, slow and unfinished story. In: Marano P, Siri M (eds) *Insurance regulation in the European Union. Solvency II and beyond*. Palgrave Macmillan
- Della Negra F (2019) *MiFID II and private law: enforcing EU conduct of business rules*. Bloomsbury Publishing
- Gortsos C (2018) *Stricto Sensu Investor Protection under MiFID II: a systematic overview of Articles 24-30*. Cambridge Scholars Publishing
- Kern A (2018) *Marketing, sale and distribution. Mis-selling of financial product. A study request by the ECON Committee*
- Kucharski B (2019) *Cywilnoprawne konsekwencje niedostosowania przez dystrybutora produktu ubezpieczeniowego do wymagań i potrzeb klienta (Civil law consequences of the non-adjustment of an insurance product by the distributor to the demands and needs of a customer)*, "Prawo asekuracyjne" v. 3/2019, Warszawa
- Malinowska K (2017) *Najlepszy interes klienta – rozważania na tle ustawy o dystrybucji ubezpieczeń (Customer's best interest – considerations against new regulations on insurance distribution)*. In: Gnela B, Szaraniec M (eds) *Dystrybucja usług ubezpieczeniowych. Wybrane zagadnienia prawne (Distribution of insurance services. Selected legal issues)*. Warsaw
- Malinowska K (2018) *Customer's best interest as a rule in insurance contracts, considerations against new regulations on insurance distribution*. In: Malinowska K, Tarasiuk A (eds) *Insurance challenges of Anno Domini 2018. Publikacja jubileuszowa AIDA 2018*, Warszawa
- Marano P (2017a) *The 'Mifidization': the sunset of life insurance in the EU regulation on insurance? Liber Amicorum for Professor Ioannis Rokas, NOMIKH BIBΛIOΘΗKH*, Athens
- Marano P (2017b) *Sources and tools of the insurance regulation in the European Union*. In: Marano P, Siri M (eds) *Insurance regulation in the European Union. Solvency II and beyond*. Palgrave Macmillan
- Mrozowska-Bartkiewicz B (2016) *Jakie zmiany dla polskiego rynku ubezpieczeń przyniesie Dyrektywa w sprawie dystrybucji ubezpieczeń? (What changes will the Directive on insurance distribution bring to the Polish insurance market?)*. *Wiadomości Ubezpieczeniowe* v. 2/2016, Warsaw
- Noussia K, Siri M (2019) *The legal regime and the relevant standards*. In: Marano P, Rokas I (eds) *Distribution of insurance-based investment products. The EU regulation and the liabilities*. Springer
- Nowak J (2018) In: Czublun P (ed) *Ustawa o dystrybucji ubezpieczeń. Komentarz. Insurance Distribution Act. Comment*. CH Beck, Warszawa
- Orlicka J (2015) *Zakaz stosowania klauzul abuzywnych i missellingu w znowelizowanej ustawie o ochronie konkurencji i konsumentów (Prohibition on the application of abusive clauses and misselling in the revised consumer and competition protection act)*. *Prawo Asekuracyjne* v. 4/2015
- Orlicki M (2016) *Projektowanie typu ubezpieczenia ("produktu ubezpieczeniowego") według rekomendacji KNF dla zakładów ubezpieczeń dotyczących systemu zarządzania produktem (Insurance type (insurance product) design pursuant to the PFSA's recommendations for insurance companies about product management system)*, *Prawo Asekuracyjne* v. 3/2016
- Orlicki M (2017) *Aksjologia dystrybucji ubezpieczeń – kryteria uznawania działań dystrybutora za zgodne z prawem i etyczne (Axiology of insurance distribution - criteria for considering the distributor's activities legal and ethical)*. In: Gnela B, Szaraniec M (eds) *Dystrybucja usług ubezpieczeniowych. Wybrane zagadnienia prawne (Distribution of insurance services. Selected legal issues)*. Warszawa
- Paś W (2018) *Obowiązek działania przez agenta ubezpieczeniowego zgodnie z najlepiej pojętym interesem klienta a jego lojalność wobec zakładu ubezpieczeń (The insurance agent's obligation to act in accordance with the customer's best interests in the context of his loyalty to the*

- insurance company). In: Malinowska K, Tarasiuk A (eds) *Insurance challenges of Anno Domini 2018. Publikacja jubileuszowa AIDA 2018*, Warszawa
- Pokrzywniak J (2018) Obowiązek rozpoznania wymagań i potrzeb klienta (Obligation to identify customer requirements and needs). In: Pokrzywniak J (ed) *Nowe zasady dystrybucji ubezpieczeń* (New rules for insurance distribution). Warsaw
- Tarasiuk A, Wojno B (2018) Analiza wymagań i potrzeb klienta w procesie dystrybucji ubezpieczeń (Demands and needs analysis in the process of insurance distribution). *Prawo asekuracyjne* 3/2018, Warszawa
- Wędrychowska-Karpińska A, Wiercińska-Krużewska A (2016) Komentarz do art. 24 ustawy o ochronie konkurencji i konsumentów (Commentary on article 24 of the act on competition and consumer protection). In: Stawicki A, Stawicki E (eds) *Ustawa o ochronie konkurencji i konsumentów* (Competition and Consumer Protection Act). Comment, wyd. II
- Wojno B (2017a) Komentarz do art. 365 ustawy o działalności ubezpieczeniowej i reasekuracyjnej (Commentary to Article 365 of the Polish act on insurance and reinsurance activity). In: Szczepańska M, Wajda P (eds) *Ustawa o działalności ubezpieczeniowej i reasekuracyjnej* (Polish act on insurance and reinsurance activity. Commentary). Warsaw
- Wojno B (2017b) Komentarz do art. 362 ustawy o działalności ubezpieczeniowej i reasekuracyjnej (Commentary to Article 362 of the Polish act on insurance and reinsurance activity). In: Szczepańska M, Wajda P (eds) *Ustawa o działalności ubezpieczeniowej i reasekuracyjnej* (Polish act on insurance and reinsurance activity. Commentary). Warsaw
- Ziemiak MP (2019) Wynagrodzenie pośrednika ubezpieczeniowego w kontekście ustawy o dystrybucji ubezpieczeń. Zagadnienia wybrane (Remuneration of insurance intermediary in the context of insurance distribution act. Selected issues). "Wiadomości Ubezpieczeniowe" v. 2/2019, Warszawa

Open Access This chapter is licensed under the terms of the Creative Commons Attribution 4.0 International License (<http://creativecommons.org/licenses/by/4.0/>), which permits use, sharing, adaptation, distribution and reproduction in any medium or format, as long as you give appropriate credit to the original author(s) and the source, provide a link to the Creative Commons licence and indicate if changes were made.

The images or other third party material in this chapter are included in the chapter's Creative Commons licence, unless indicated otherwise in a credit line to the material. If material is not included in the chapter's Creative Commons licence and your intended use is not permitted by statutory regulation or exceeds the permitted use, you will need to obtain permission directly from the copyright holder.