

**THE NATURE AND ART OF
FINANCIAL SUPERVISION
VOLUME VI**

¹⁹**CONDUCT SUPERVISION**
THE DEMANDS AND NEEDS ASSESSMENT



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Table of Abbreviations

Alls	Ancillary Insurance Intermediaries
EIOPA	European Insurance and Occupational Pensions Authority
EU	European Union
IDD	Insurance Distribution Directive
IBIP	Insurance-based Investment Product
MFSA	Malta Financial Services Authority
TIIs	Tied Insurance Intermediaries

Introduction

An Overview

Article 20(1) of the Insurance Distribution Directive ('IDD') provides that any contract proposed shall always be consistent with the demands and needs of the client. Under the IDD, all insurance undertakings and insurance intermediaries carrying out insurance distribution activities (hereinafter, referred to as 'insurance distributors') are required to specify the demands and needs of their clients based upon information obtained therefrom. These requirements have been transposed in Chapter 4 of the Conduct of Business Rulebook. Accordingly, insurance distributors are expected to take active steps to obtain information from their clients to be in a position to carry out this assessment. Insurance distributors shall then consider this information in the context of the characteristics and features of the insurance products they have on offer in order to ensure that the insurance policy they finally propose or recommend to a client is consistent with those client's demands and needs. Insurance distributors shall not offer clients any products which do not meet their demands and needs.

Therefore, the assessment of client demands and needs by insurance distributors, prior to the conclusion of the contract, is a key part of the insurance distribution process. The demands and needs assessment provides protection for clients by seeking to minimise the risk of harm to consumers resulting from their purchasing products which do not meet their needs. This assessment is required to be carried out prior to the sale of all types of insurance contracts, not only Insurance Based Investment Products (IBIPs)¹.

The MFSA's Supervisory Work

The MFSA is strongly committed to ensure that conduct of business-related requirements are properly and consistently implemented throughout all the insurance distribution channels. Due to their relevance in terms of consumer protection, the MFSA considers that it is of utmost importance that requirements relating to the demands and needs assessment are properly implemented and applied.

The MFSA has been carrying out supervisory work in the area of insurance conduct supervision covering various areas, including also the carrying out of demands and needs assessment by insurance distributors. This includes thematic inspections carried out to intermediaries, including brokers, during 2020 and 2021, with a view to

¹ Art. 30 of the IDD (in the context of IBIPs) applies "*without prejudice*" to the demands and needs test covered by Art. 20(1) of the IDD. This is also specified in Recital 7 of Delegated Regulation 2017/2359.

assess adherence with relevant requirements of the IDD and the Conduct of Business Rulebook ('COBR').

The Authority's findings in this context evidenced a lack of adequate understanding by insurance distributors of the elements of the demands and needs assessment and the manner in which it should be carried out. In this context, the purpose of this Circular is to clearly set out the Authority's expectations with respect to the carrying out of the demands and needs assessment by insurance distributors, prior to the conclusion of insurance contracts with their respective clients.

Scope, Purpose and Structure of this Publication

This document is addressed to insurance undertakings and insurance intermediaries regulated by the MFSA, carrying out insurance distribution. Its purpose is to provide guidance and set out the MFSA's expectations in the context of the demands and needs assessment which insurance distributors are required to make in accordance with their regulatory requirements.

Section 1 of this Document sets out the MFSA's explanations and expectations in the context of the requirement on insurance distributors to assess their clients' respective demands and needs prior to the conclusion of a contract. Section 2 indicates the way forward with respect to these expectations, including the next steps which the Authority may take on this matter.

Section 1: MFSA Expectations with Respect to the Demands and Needs Assessment

1.1 What is the Demands and Needs Assessment?

In terms of Article 20(1) of the IDD, all insurance distributors are required to take a more active role in identifying their clients' demands and needs, and shall ensure that any insurance policy proposed to clients meets those demands and needs.

Article 20(1) of the IDD stipulates that, prior to the conclusion of an insurance contract, the insurance distributor shall specify, ***on the basis of information obtained from a client***, the specific demands and the needs of that client; and shall provide the client with objective information about the insurance product in a comprehensible form to allow that client to make an informed decision. The insurance distributor shall:

- (a) ensure that any contract proposed by it shall meet the client's insurance demands and needs;
- (b) where advice is provided prior to the conclusion of any specific contract, provide the client with a personalised recommendation (explaining why a particular product would best meet that client's personal circumstances); and
- (c) modulate such process in accordance with the complexity of the insurance product being proposed and the type of client.

The above requirements, which have been transposed into Rules R.4.4.78 to R.4.4.80 in Chapter 4 of the COBR', mean that insurance distributors cannot simply offer products to clients through generic statements about the type of needs each product will meet. Thus, for example, inserting a generic statement on the product documentation stating that such product meets the demands and needs of clients with a particular profile would not be sufficient since such a statement would not be provided "***on the basis of information obtained from the client***", as is required in terms of the IDD requirements.

1.2 Why should a Demands and Needs Assessment be carried out?

Insurance distributors are required to ensure that they are distributing the right products to the right clients. The insurance distributor's assessment of the information obtained from the client, against the relevant insurance products available

on the market, will identify which product(s) would best suit the particular client insofar as his/her particular demands and needs are concerned.

1.3 Who is required to carry out such a Demands and Needs Assessment?

The demands and needs assessment is required to be undertaken by all insurance undertakings and insurance intermediaries, including Tied Insurance Intermediaries ('TIIs') and Ancillary Insurance Undertakings ('AIs') carrying out insurance distribution activities.

With respect to TIIs, and AIs, entities appointing such intermediaries are also expected to have measures in place to ensure that appointed TIIs and AIs distributing their products consider adequately and sufficiently the demands and needs of their clients, on the basis of information obtained from their clients, before the proposal of an insurance product is made.

Accordingly, such entities appointing such intermediaries shall monitor the manner in which TIIs and AIs are carrying out a demands and needs assessment for every policy they sell. For each insurance product distributed, insurance undertakings are expected to provide their appointed TIIs and AIs with guidance as to how such demands and needs assessments should be carried out and may also consider providing standard templates to assist in the pre-contractual phase of acquiring useful and pertinent information from the client in relation to the type of product offered.

As part of their monitoring activities over their TIIs and AIs, entities appointing such intermediaries are also expected to monitor (on a risk-based sample basis) that their TIIs and AIs are carrying out the demands and needs assessment in a proper manner and that the products being offered to the client do in fact match the particular client's demands and needs.

1.4 When should a Demands and Needs Assessment be carried out?

A demands and needs assessment should be undertaken **before** a product is offered to a client and, therefore, before a particular product is identified and consequently **before** the relative proposal form can be completed. The demands and needs assessment is a stage which is separate and distinct from the completion of a proposal form. In terms of the sales journey, this assessment should be carried out

before any products are offered to a client and therefore, before the relative proposal form is referred to for completion.

In the context of the demands and needs assessment, the questions asked to clients may be similar to those asked for the purposes of underwriting (and which are usually found in a proposal form). However, the purpose of this assessment is not for underwriting and therefore, replies provided by clients should be assessed to identify the product(s) which would best meet the client's demands and needs and not to establish whether the client's risk falls within the insurer's underwriting parameters.

Information received from the client in the context of the demands and needs assessment may then be utilised to complete the relative proposal form – once a product(s) has been identified by the insurance distributor and chosen by the client.

Moreover, reliance by the insurance distributor on the exclusive use of a specific product's proposal form as a substitute for a demands and needs assessment is not acceptable, as this would mean that a product would have already been selected for the client before their demands and needs assessment is performed.

It is to be emphasised that the requirement to carry out the demands and needs assessment applies regardless of the distribution modality; and applies to **all types** of insurance contracts irrespective of whether the products:

- (a) are complex or non-complex;
- (b) are provided with or without advice;
- (c) relate to general or long-term insurance.

Pursuant to Article 20(1) of the IDD, any insurance contract proposed to the client must always be consistent with the demands and needs of the said client. Accordingly, an insurance distributor shall refrain from selling insurance product(s) where:

- (a) these do not correspond to the client's demands and needs; or
- (b) where the insurance distributor is unable to ensure (and demonstrate) that the product corresponds to the specific client's demands and needs, due to the refusal by the latter to provide the information requested.

The above applies even where the client falls within the target market identified for the relevant insurance product(s).

The demands and needs assessment is required to be carried out for all types of insurance products, that is, for both general and long-term business. In respect of long-term business, insurance distributors are requested to ensure that the demands and needs assessment is carried out for both IBIPs and pure protection products.

In the context of IBIPs, a demands and needs assessment is required in order to identify whether the clients' needs are better addressed by, for example, a 'with profits' rather than a unit-linked policy. Once this is decided, then – unless the conditions for an execution-only transaction subsist – a suitability assessment or an appropriateness assessment would also need to be carried out. This is required so that the insurance distributor can assess whether the particular product(s) (identified as meeting the client's demands and needs) that it offers is suitable or appropriate for the client, as applicable, in his/her particular circumstances.

In the case of online sales, a demands and needs assessment is still required to be carried out by the insurance distributor and relevant tools should be tailored for such the medium utilised. This may be achieved by requesting the client to reply to a number of questions relating to, inter alia, what the client is expecting out of the insurance product under consideration, and then have an algorithm in place which ensures that the product being offered would match the client's demands and needs, in accordance with the replies provided to the above-mentioned questions.

Renewals

The demands and needs assessment is also required to be carried out upon policy renewals. In this regard, insurance distributors are expected to **clearly** request their clients, through the renewal notice, to inform them whether there were any changes in their personal circumstances which would affect the risk insured (for instance, new improvements to a home); or if there have been changes to the risk insured itself during the last period of insurance, which would need to be communicated by the client to the insurance distributor. In such cases, a fresh demands and needs assessment would be required to be carried out by the insurance distributor prior to the renewal being effected.

This means that if an insurance distributor includes in the renewal notice a reminder to the client that he or she is required to update the insurance distributor with any changes to their circumstances or to the risk insured, and the client does not advise of any such changes, then the insurance distributor would be able to rely on the demands and needs assessment carried out when the last policy was issued. If on the other hand, the client advises the insurance distributor that there have been changes in his or her circumstances or to the risk insured, a new demand and needs assessment needs to be carried out by the insurance distributor prior to renewal.

1.5 How should a Demands and Needs Assessment be carried out?

The IDD clearly states that the demands and needs assessment is to be made on the basis of information obtained from the client. This will entail a discovery exercise which would be typically done through a set of questions posed to the client by the insurance distributor. In this regard, the MFSA considers that the obligation to perform a demands and needs assessment can be carried out in a number of ways. The manner in which a demands and needs assessment is carried out and the extent thereof (that is, adopting a proportional approach depending on the type of service provided and the complexity of the insurance product(s) under consideration) is up to the insurance distributor to determine.

In order to comply with the requirement to specify the clients' demands and needs, there has to be an actual assessment of the client's demands and needs, that is a positive action on the part of the insurance distributor in order to specify, on the basis of information obtained from the client, the demands and the needs of that client. Therefore, the said requirement may not be satisfied by the mere provision of the policy quotation and, or the provision of product information/documentation, such as the Insurance Product Information Document. Indeed, the provision of such information should follow the assessment of the demands and needs.

The onus is on the insurance distributor to ensure that the necessary information from clients is gathered and that the demands and needs assessment is actively made on the basis of that information.

It is not adequate for the insurance distributor to place reliance on client-facing members of staff to ask impromptu questions during informal discussions with the client. In this regard, the MFSA expects that a structured and formal assessment is made in order to ensure consistency in the level of information gathered from all clients by all members of the insurance distributors' staff; and so that compliance with the relevant requirements in relation to demands and needs can be adequately demonstrated.

In this context, insurance distributors are expected to have policies and procedures in place to be followed by its members of staff who would be offering insurance products to clients. Furthermore, it is expected that the insurance distributor's staff are specifically guided and trained as to how to analyse the information provided by clients in order to carry out a demands and needs assessment before offering policies to clients.

It is acceptable to adopt the use of questionnaires for this purpose, but this is not mandatory, provided that sufficient information is collected from clients through other means.

The insurance distributor is expected to consider requesting information regarding the personal characteristics and the insurance needs of the client, which would include, by way of example and where applicable (and depending on the type of policy under consideration in terms of its level of cover, costs, exclusions, deductibles and other terms and conditions):

- (a) age;
- (b) health condition;
- (c) employment;
- (d) how much by way of deductible the client is prepared to pay;
- (e) the type of cover the client is seeking;
- (f) any insurance coverage already in effect;
- (g) the type and usage of the risk which is going to be the subject of the contract;
and
- (h) the characteristics and complexity or otherwise of the offered product.

This information shall enable the insurance distributor to assess whether certain products can be offered or not according to their capacity to meet the demands and needs of the client. Therefore, following the gathering of the relative information from the client, the insurance distributor would need to take into account a policy's level of cover, the costs, as well as the relevant exclusions, deductibles and other limitations and conditions, in order to ensure that the policy or policies offered would meet the particular demands and needs of the specific client.

1.6 When should a Demands and Needs Statement be provided?

On the basis of the information gathered and taking into account the type of client and the nature and complexity of the product offered, the insurance distributor shall, in a clear and comprehensible manner, provide the client with objective information on the product, illustrating its characteristics, duration, costs, coverage limits and any other relevant elements to enable the client to make an informed decision.

In this regard, insurance distributors are expected to provide the client with simple, clear and understandable information about the basis on which an insurance product is offered and how it relates to their demands and needs. Insurance distributors are expected to provide their clients with a demands and needs statement. Such statement would normally include:

- (a) a record of the requirements the insurance product is intended to meet;
- (b) the type of product that is being purchased;
- (c) whether it has provided advice (*please refer to the below for an explanation of what constitutes advice*), with respect to on the product; and
- (d) the reasons why the particular product has been offered to the client, that is, how the product offered would meet the client's demands and needs on the basis of the information provided by the client to the insurance distributor for this purpose.

The content of a demands and needs statement, and the process for its issue, differ somewhat according to whether the Insurance distributor is:

- (a) only arranging for the client to enter into the insurance policy in question, without providing advice or a personal recommendation on the choice of the policy; or
- (b) providing advice or a personal recommendation on the insurance policy in question.

If the insurance distributor is only arranging the insurance policy in question (that is, **no personal recommendation** is made to the client); the statement should:

- (a) set out the client's insurance requirements as the client has disclosed them to the insurance distributor (that is, set out what the client wants from the product) and how these needs will be addressed by the product(s) being offered, taking into account the product's cover, exclusions, deductibles and other product elements; and
- (b) state that the insurance distributor has not provided the client with advice or a personal recommendations with respect to the policy.

On the other hand, if the insurance distributor is **providing advice and hence, providing a personal recommendation** on the insurance policy in question, which can be an IBIP or a non-IBIP (*please refer to the below for an explanation of what constitutes advice*), the insurance distributor should then provide the client with a written statement that:

- (a) sets out their demands and needs based on the information provided by the client;
- (b) confirms that the insurance distributor is recommending a particular policy; and
- (c) explains the reasons for the said recommendation, that is, why the Insurance distributor is recommending that particular policy as the most suitable for the client among those on offer.

In any event, the demands and needs statement shall be given in good time and before the contract is concluded. There is no prescribed format and the statement may take the form of a summary note of the discussion, or a suitably completed checklist or even a statement highlighting why the product being offered is deemed to be in line with the client's demands and needs. This statement may be provided as part of the pre-contractual documentation provided to the client (for instance, as part of the quotation) or as a separate document.

In principle, the demands and needs statement is expected to be provided in a durable medium within the meaning of the COBR. However, if a client so requests, or if the client requires immediate insurance cover, the information may initially be provided orally. The Insurance distributor is nevertheless expected to follow-up with written documentation immediately after the conclusion of the contract.

The insurance distributor is also expected to ensure that, in any documentation (including the demands and needs statement) which it may request clients to sign in relation to the demands and needs assessment, the onus of the assessment of the demands and needs is not to be shifted in any manner onto the client. Accordingly, care shall be taken by the insurance distributor when drafting such documents so as to ensure that the client is not in any way assuming responsibility for the demands and needs assessment or for the personal recommendation made since both the demands and needs assessment and personal recommendations (if any) are always deemed to be the responsibility of the insurance distributor. Accordingly, requesting or prompting the client to confirm in any manner that the contract chosen is in line with his/her demands and needs is not acceptable². Furthermore, any such documents would also be expected to be also signed by a representative of the insurance distributor if the latter requests the client to sign such documents.

In the context of insurance brokers, unless these wish to provide personal advice (that is, via a personal recommendation), these are expected to consider a sufficiently large number of policies available on the market with a view to identify those policies which would meet the client's demands and needs. A demands and needs statement would be required to be provided to the client for each policy so identified, such that the client would be in a position to choose the policy under which to bind cover out of those indicated by the broker.

What is Advice?

Advice refers to the provision of a personal recommendation to a client, either upon their request or at the initiative of the insurance distributor, in respect of one or more

² [Vide EIOPA's Report on the Application of the IDD published 6 January 2022, EIOPA-BoS-21/581](#)

insurance contracts. A personal recommendation would be taken to involve the recommendation provided to a particular client to purchase a particular product after considering the personal circumstances of such client. Accordingly, a recommendation is not a 'Personal Recommendation' if it is issued exclusively to the public (for instance, through an advert or newspaper article).

The insurance distributor is expected to be clear with the client as to whether it is providing advice or otherwise.

It is important to note that while advice may be provided both with respect to IBIPs and non-IBIPs, the formal suitability/appropriateness assessments are only required under Article 30 of the IDD in the context of the sale of IBIPs.

If the insurance distributor is arranging insurance policies only, the insurance distributor is in effect taking the clients' orders, after carrying out a demands and needs assessment, and effecting the purchase of the insurance product chosen by the client in line with their wishes.

In this scenario, when providing information about the product in question, it is important to ensure that no advice is provided unintentionally by such distributor. This could occur, for instance, if the client asks, "what do you think?" or "which would you go for?". In these cases, if the clients poses such questions, if the distributor does not wish to provide advice, it should inform the client that they are not in a position to give a personal recommendation (that is, as to whether the product is suitable in the client's particular circumstances) and that as an insurance distributor, they have merely assessed whether that product meets the client's demands and needs.

As indicated above, the demands and needs statements needs to be clear as to the basis on which the service is being provided by the insurance distribution service (that is, advisory or non-advisory).

1.7 What Records Should be Kept in relation to the Demands and Needs and Assessment?

The demands and needs assessment carried out by the insurance distributor is expected to be formalised and a record evidencing the manner in which it has been carried out, and the relative result is to be maintained. Accordingly, insurance distributors are expected to keep sufficient records with respect to:

- (a) the questions asked for the purposes of the demands and needs assessment and the respective replies provided by the client;
- (b) the result of the assessment which is to be communicated to the client;
- (c) a copy of the demands and needs statement provided to the client.

TIIIs and AIIIs are also expected to keep the above-mentioned records in order to enable the entities appointing them and on whose behalf they act, to monitor the extent and the manner in which such demands and needs assessments are being carried out by their respective appointed TIIIs and AIIIs.

In general, effective record-keeping will enable the insurance distributor's compliance function to monitor the extent and manner in which the demands and needs test is being carried out and to demonstrate that it is actually being carried out. Accordingly, it is expected that this monitoring – including, where applicable with respect to TIIIs and AIIIs – would feature in the insurance distributor's compliance plan, on an ongoing basis.

Way Forward and Next Steps

The MFSA has engaged and is engaging on a bilateral basis with the entities at which it has conducted an inspection in the context of conduct-related matters, including the carrying out of the demands and needs assessment.

All insurance distributors, including those which have not been subjected to an MFSA inspection, are expected to come in line with the MFSA's guidance and expectations as outlined in this document.

Moreover, it is also to be highlighted that the MFSA's guidance, principles and expectations as outlined in this document may in due course be incorporated as new rules, and/or guidance within the COBR. It is strongly recommended that insurance distributors also refer to the [Q&As](#), published on EIOPA's website, some of which also cover this matter.

The supervisory expectations contained in this document are without prejudice to any possible amendments to the IDD and to any other expectations or guidance which may be published by EIOPA in the context of the demands and needs assessment in due course.

Contacts

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