

*SUMMARY OF OUTPUTS FROM  
PUBLIC CONSULTATION*

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**STANDARDS OF EXPERTISE  
FOR DISTRIBUTORS OF PRODUCTS  
IN THE FINANCIAL MARKET**

Ministry of Finance of the Czech Republic

29 July 2008

**MINISTRY OF FINANCE OF THE CZECH REPUBLIC**  
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### **Preamble**

In December 2007, the Ministry of Finance (MF) issued the “Standards of Expertise for Distributors of Products in the Financial Market” for public consultation. The consultation material was the first step in implementing one of the objectives stipulated in the Framework Policy of the Ministry of Finance on Consumer Protection in the Financial Market, which is **ensuring that the distributors of financial products have a certain level of knowledge and skill.**

The **objective** of the public consultation was to acquaint the public with the MF’s first proposal for the future setup of the system of requirements on the expertise of distributors of financial products and services. The presented proposal did not anticipate any specific future form and served to initiate discussion.

Expertise for the purposes of the mentioned system is understood by the MF to be the **expertise** necessary to distribute financial products as well as the **know-how** to apply the expertise in practice. In the MF’s opinion, the distributors’ knowledge and skill should be demonstrated in various areas of the financial market and economics in general, and an integral part thereof should also be **knowledge of ethics principles** applicable to customer relationships.

According to an analysis performed by the MF, the requirements on the expertise of the distributors contained in current legislation are markedly **unbalanced**. Certain sectors (such as the capital market and distribution of financial instruments) are subject to strict regulation in this area, whereas there are practically no requirements on other areas of no less importance (such as distribution of mortgages). The MF sees this state as being problematic and plans to focus its next steps on making the conditions equal across the financial market. This, however, does not mean applying the rules of one sector

to another sector without changing them. **The objective is to find a solution that will ensure comparable conditions in terms of consumer awareness and protection in the entire market.**

When contemplating the expertise requirements, the MF came up with a so-called **production-function approach**. Until then, the rules were proposed for each sector in isolation (e.g., for the capital market, for insurance). According to the new approach, regulation should not be primarily aimed at a specific sector and group of financial institutions, but, conversely, on a **group of financial products** whose economic raison d'être and financial function is the same for the consumer (e.g., products for investing available funds).<sup>1</sup> The European Commission, as part of so-called substitutable product activity, is taking the same approach to reviewing the rules in the financial market.<sup>2</sup>

The described approach stems from current developments and trends in the financial market. Integrating financial institutions are offering to clients more and more products that combine the marks of products from across sectors (e.g., investment life insurance, structured deposits, leasing, and the like), with the requirements on expertise differing in each market sector, however. The undesirable accompanying feature of such legislative status quo is – from the perspective of both consumer protection and financial market development – so-called **regulatory arbitrage**.<sup>3</sup> Unifying distribution rules (i.e., expertise requirements as well) will contribute to restricting distribution.

In the consultation material, the MF proposed and emphasised an interest in the **active participation of professional associations**, both when formulating

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<sup>1</sup> This group can include, e.g., capital and investment life insurance, share funds, structured deposits, supplementary pension insurance, and other savings and investment products.

<sup>2</sup> Retail investment products – Reviewing the adequacy of EU product disclosure and distribution rules (European Commission, Internal Market and Services DG).

<sup>3</sup> Regulatory arbitrage is a form of market distortion where financial institutions and agents focus their offer on those products and services that are – compared to others – subject to less strict rules stipulated by legislation (e.g., rules for providing information to clients, requirements on distributor expertise, and the like)

the main theses and when implementing their own system of ensuring the expertise of distributors in practice. In such proposed model, the MF should, in cooperation with the CNB, determine a certain minimum framework, where its specification and the implementation of the standards themselves could be transferred to professional associations.

In connection with the receipt of comments and suggestions, the MF also initiated a number of **meetings** with certain market representatives. The content of such meetings was to clarify the mutual positions towards its own consultation materials and to discuss the broader context of the State's approach to consumer protection policies in the financial market.

The purpose of this document is to summarise the main conclusion of this first phase of consultations and outline the MF's next steps in securing expertise in the financial market.

### **Public consultation participants**

The MF received a response from a total of 15 entities, mainly professional associations. The following box contains an overview of these entities.

#### **Box 1 – Public consultation participants**

- Association of Czech Insurance Brokers (*Asociace českých pojišťovacích makléřů*)
- Association of Financial Intermediaries and Financial Advisers of the Czech Republic (*Asociace finančních zprostředkovatelů a finančních poradců ČR*)
- The Association of Pension Funds of the Czech Republic (*Asociace penzijních fondů ČR*)
- Astorie a.s. – financial advisers
- Banking Institute/ College of Banking (*Bankovní institut – vysoká škola*)
- Brzobohatý Brož & Honsa – law firm
- Czech Association of Securities Traders (*Česká asociace obchodníků s cennými papíry*)
- Czech Insurance Association (*Česká asociace pojišťoven*)
- Czech Banking Association (*Česká bankovní asociace*)
- Czech National Bank (*Česká národní banka*)
- Czech Financial Arbitrator (*Finanční arbitr ČR*)
- IMG, a.s. – financial advisers
- Masaryk University (*Masarykova univerzita*)
- Consumer Defence Association (*SOS - Sdružení obrany spotřebitelů*)
- Union of financial intermediaries and consultants (*Unie společností finančního zprostředkování a poradenství*)

***Main outputs of the public consultation***

1. The general conclusion from both the consultation process and the subsequent meetings is **confirmation of the correctness of the MF's intention to address** the issue of the expertise of distributors in the financial markets. Some of the addressed partners proposed immediate commencement of specific steps, themselves publicly announcing this intention and stating to work on it on their own initiative. In the case of the solution in the form of self-regulation (auto-regulation), the MF should contribute to ensuring that the approach taken by each stakeholder in the market is uniform and leads to a common goal. On the other hand, the second group of participants in the discussion was not convinced of the urgency of this problem. The reserved stance toward the need for immediate changes stems from the opinion that in a number of sectors the current situation is sufficient and that it would be more appropriate to wait for specific measures at the pan-European level, which will then affect the method of regulation of the Czech market. The majority of consultation participants agreed that the best way to proceed would be to cooperate on the basis of a professional working group and showed interest in participating actively in it.

2. It also stemmed from the consultations that the pivotal prerequisite for actually starting contemplation of the outline of the new system to ensure expertise is a discussion about the need for a new regulation on business licences and registration of subjects in the financial market. Here there will be a key debate on regulating access to the sector for hitherto unregulated entities, namely non-banking creditors. The need to set new rules also stems from, inter alia, the requirements of Directive 2008/48/EC, on credit agreements for consumers.<sup>4</sup>

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<sup>4</sup> Article 20 of the Directive states that “Member States shall ensure that creditors are supervised by a body or authority independent from financial institutions, or regulated.”

3. The MF's proposal to set standards of expertise for all types of distributors of financial services, i.e., not only for financial intermediaries but also for regular financial institution employees who sell financial products to retail clients (branch office workers, persons responsible for direct sales channels and the like), was contentious for some of the addressed parties. The main argument of opponents of additional regulation in the case of employees was the sufficiency of current training that these workers undergo.

4. An important aspect of the MF's proposal also became the new product-function approach to regulating the distribution of financial products (described above). Opinions on this approach differ greatly among the addressed financial market entities, with the proponents of a more reserved approach calling attention mainly to the complexity of its implementation into current Czech legislation (the current regulation stipulates the rules for the most part in an isolated manner for each sector). Here the MF calls attention to the fact that the product-function approach is mainly a new method of thinking when creating the rules and does not necessarily mean an intention to regulate through one general law.

5. The consultation participants further agreed to create a multiple access system of requirements on expertise, where more moderate requirements exist on mediating sale and stricter requirements exist on comprehensive financial advisory.

6. As part of related consultations with professional associations in the insurance sector,<sup>5</sup> agreement was voiced with the MF's approach to expertise, i.e., with the need to set the requirements on proving not only expertise but also know-how and the expectations on the ethical behaviour of the distributors of financial services. Certain associations expressly stated that they demand

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<sup>5</sup> MF's consultation questions related to certain aspects of distribution of insurance products (MF, 10 June 2008)

making it more difficult to acquire a licence to do business in the insurance sector, so as to ensure that testing was not only a formality, thereby ensuring that the quality of distribution among the participants is high.

7. Other comments that the MF received as part of the first phase of consultation and that will be the topic of discussions with the financial market regarded, for example, the way expertise is acquired, the selection of suitable examples from abroad, possibilities and functionality of self-regulation elements in the systems, the needs for analysis of the factual state of expertise in the financial market, and so on.

### ***Next steps***

In connection with the completed first phase of consultation, the MF will continue with the professional consultations on the basis of a special working group comprising market representatives, the MF, the CNB, and consumers. The group should be created this autumn. The objective will be to address in more detail the specific issues outlined in the public consultations and finding the most suitable options to resolve them. The MF will inform experts and the general public on developments on work in the area on an ongoing basis.