Product Intervention and Product Governance Sourcebook (PROD)
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Chapter 1

Product Intervention and Product Governance Sourcebook (PROD)
1.1 Application and purpose

Purpose

1.1.1 The purpose of PROD is to improve firms’ product oversight and governance processes and to set out the FCA’s statement of policy on making temporary product intervention rules.

1.1.2 Product oversight and governance refers to the systems and controls firms have in place to design, approve, market and manage products throughout the products’ lifecycle to ensure they meet legal and regulatory requirements.

1.1.3 Good product governance should result in products that:

(1) meet the needs of one or more identifiable target markets;

(2) are sold to clients in the target markets by appropriate distribution channels; and

(3) deliver appropriate client outcomes.
1.2 Application of PROD 2

1.2.1 PROD 2 sets out the FCA’s approach to issuing temporary product intervention rules. It is of relevance to all firms.
1.3 Application of PROD 3

General: Who? What?

1.3.1 PROD 3 applies to

(1) a MiFID investment firm;
(2) a CRD credit institution;
(3) a MiFID optional exemption firm; and
(4) branches of third country investment firms; with respect to:
(5) manufacturing financial instruments and structured deposits; and
(6) distributing financial instruments, structured deposits and investment services.

Note: articles 1(3), 1(4), 16(3), 24(2) and 41(2) of MiFID

Other firms manufacturing or distributing financial instruments or structured deposits

1.3.2 Other firms which manufacture or distribute financial instruments or structured deposits should take account of PROD 3 as if it were guidance on the Principles and other relevant rules and as if “should” appeared in PROD 3 rules instead of “must”.

Eligible counterparty business

1.3.3 PROD 3.3.1R does not apply to eligible counterparty business.

Note: article 30(1) of MiFID

Where?

1.3.4 PROD 3 applies to a firm with respect to activities carried on from an establishment maintained by it, or its appointed representative, in the United Kingdom.

1.3.5 (1) PROD 3 also applies to a firm with respect to activities from an establishment overseas with a client in the United Kingdom.
(2) But PROD 3 does not apply to those activities if the office from which the activity is carried on were a separate person and the activity:

(a) would fall within the overseas persons exclusions in article 72 of the Regulated Activities Order; or

(b) would not be regarded as being carried on in the United Kingdom.

**EEA territorial scope rule: compatibility with European law**

1.3.6 R

(1) The territorial scope of this sourcebook is modified to the extent necessary to be compatible with European law (see PROD 1.3.7G to PROD 1.3.10G for guidance on this).

(2) This rule overrides every other rule in this sourcebook.

**Effects of the EEA territorial scope rule**

1.3.7 G

One of the effects of PROD 1.3.6R is to override the application of this sourcebook to the overseas establishments of EEA firms in circumstances covered by MiFID.

1.3.8 G

The guidance in this chapter provides a general overview only and is not comprehensive.

1.3.9 G

When considering the impact of a directive on the territorial application of a rule, a firm will first need to consider whether the relevant situation involves a non-UK element. PROD 1.3.6R is unlikely to apply if a UK firm is doing business in a UK establishment for a client located in the United Kingdom in relation to a UK product, in other words PROD 3 will apply to the UK firm. However, if there is a non-UK element, the firm should consider whether:

1. it is subject to the directive (in general, directives only apply to UK firms and EEA firms, but the implementing provisions may not treat non-EEA firms more favourably than EEA firms);

2. the business it is performing is subject to the directive; and

3. the particular rule is within the scope of the directive.

If the answer to all three questions is ‘yes’, PROD 1.3.6R may change the application of the rules in this sourcebook.

1.3.10 G

When considering a particular situation, a firm should also consider whether two or more directives apply.

**MiFID: effect on territorial scope**

1.3.11 G

PERG 13 contains general guidance on the persons and businesses to which MiFID applies.
1.3.12 For a UK MiFID investment firm, rules in this sourcebook that are within the scope of MiFID generally apply to its MiFID business carried on from an establishment in the United Kingdom. They also generally apply to its MiFID business carried on from an establishment in another EEA State, although in the case of rules that implement article 24(2) MiFID only where that business is not carried on within the territory of that EEA State. Where a MiFID investment firm carries on MiFID business from a branch in another EEA State, organisational requirements, including rules implementing product manufacture obligations under article 16 MiFID are home state requirements and therefore FCA responsibility (see SUP 13A Annex 1G).

[Note: see articles 34(1) and 35(1) and (8) of MiFID]

1.3.13 For an EEA MiFID investment firm, rules in this sourcebook that are within the scope of MiFID generally apply only to its MiFID business if that business is carried on from an establishment in, and within the territory of, the United Kingdom and only to the extent that the rules implement article 24(2) of MiFID.

[Note: see articles 35(1) and (8) of MiFID]

Electronic Commerce Directive: effect on territorial scope


Interaction of PROD 3 and the RPPD Guide

1.3.15 A firm to which PROD 3 applies need not apply the guidance in RPPD for matters covered by PROD if the firm has complied with PROD 3.
1.4 Application of PROD 4

1.4.1 PROD 4 applies to:

(1) an insurance intermediary; and

(2) an insurer,

with respect to:

(3) manufacturing insurance products; and

(4) distributing insurance products.

[Note: articles 1(2) and 25 of the IDD]

1.4.2 In PROD an insurance product may be read as being a reference to the product for distribution to customers generally and is not intended to refer to each individual contract of insurance being sold or underwritten (unless the context indicates otherwise).

1.4.3 PROD 4 does not apply in relation to the manufacturing or distributing of:

(1) a contract of large risks, or

(2) a reinsurance contract.

[Note: article 25(4) of the IDD]

When an intermediary may be considered to be manufacturing

1.4.4 For the purposes of Article 25(1) of Directive (EU) 2016/97, insurance intermediaries shall be considered manufacturers where an overall analysis of their activity shows that they have a decision-making role in designing and developing an insurance product for the market.

A decision-making role shall be assumed, in particular, where insurance intermediaries autonomously determine the essential features and main elements of an insurance product, including its coverage, price, costs, risk, target market and compensation and guarantee rights, which are not substantially modified by the insurance undertaking providing coverage for the insurance product.
3(3) Personalisation of and adaptation of existing insurance products in the context of insurance distribution activities for individual customers, as well as the design of tailor-made contracts at the request of a single customer, shall not be considered manufacturing.

[Note: article 3 of the IDD POG Regulation]

1.4.5 The effect of ■ PROD 1.4.3EU and ■ PROD 1.4.6R is that an insurance intermediary needs to consider if it is manufacturing an insurance product and, if so, should comply with ■ PROD 4.2 (Manufacture of insurance products).

Effect of provisions marked “EU”

1.4.6 (1) Subject to (2) and ■ PROD 1.4.3R, provisions in this section and in ■ PROD 4 marked “EU” apply to firms manufacturing or distributing insurance products, but to whom the IDD POG Regulation does not apply, as if they were rules.

(2) For the purposes of (1), a word or phrase used in the IDD POG Regulation and referred to in column (A) has the meaning indicated in Column (B) of the table below:

<table>
<thead>
<tr>
<th>(a)</th>
<th>(b)</th>
</tr>
</thead>
<tbody>
<tr>
<td>“Article 17(1) of Directive (EU) 2016/97”</td>
<td>ICOBS 2.5.1R, in relation to a non-investment insurance contract, or COBS 2.1.1R, in relation to a life policy</td>
</tr>
<tr>
<td>“Article 25(1) of Directive (EU) 2016/97”</td>
<td>PROD 4.2.1R and PROD 4.2.2R</td>
</tr>
<tr>
<td>“Article 8(2)”</td>
<td>PROD 4.2.30EU</td>
</tr>
<tr>
<td>“competent authorities”</td>
<td>FCA</td>
</tr>
<tr>
<td>“customer” and “potential customer”</td>
<td>customer</td>
</tr>
<tr>
<td>“Directive (EU) 2016/97”</td>
<td>IDD</td>
</tr>
<tr>
<td>“insurance-based investment products”</td>
<td>insurance-based investment products</td>
</tr>
<tr>
<td>“insurance distribution activities” and “distribution activities”</td>
<td>insurance distribution activities</td>
</tr>
<tr>
<td>“insurance distributor”</td>
<td>distributor</td>
</tr>
<tr>
<td>“insurance intermediary”</td>
<td>insurance intermediary</td>
</tr>
<tr>
<td>“insurance undertaker”</td>
<td>insurer</td>
</tr>
<tr>
<td>“manufacturer” and “manufacturers within the meaning of Article 2 of this Delegated Regulation”</td>
<td>manufacturer</td>
</tr>
<tr>
<td>“manufacturing”</td>
<td>manufacturing</td>
</tr>
<tr>
<td>“shall”</td>
<td>must</td>
</tr>
</tbody>
</table>

(3) In this sourcebook, where a reproduced provision of an article of the IDD POG Regulation refers to another part of the IDD POG Regulation, that other provision must also be read with reference to the table in (2).
1.4.7  **R**  ■ PROD 4 applies to a firm with respect to activities carried on from an establishment maintained by it, or its appointed representative, in the United Kingdom.

[Note: article 7(2) of the IDD]

**EEA territorial scope rule: compatibility with European law**

1.4.8  **R**  (1) The territorial scope of ■ PROD 4 is modified to the extent necessary to be compatible with European law.

(2) This rule overrides every other rule in this sourcebook.

**Electronic Commerce Directive: effect on territorial scope**

1.4.9  **G**  The rules and guidance on the E-Commerce Directive in ■ ICOBS 1 Annex 1, Part 3, paragraph 1.2R and Part 4 paragraph 8, and in ■ COBS 1 Annex 1, Part 2, paragraph 1.2R and Part 3, paragraph 7, apply equally in relation to the rules in ■ PROD 4.

**Interaction of PROD 4 and the RPPD Guide**

1.4.10  **G**  A firm to which ■ PROD 4 applies need not apply the guidance in RPPD for matters covered by PROD if the firm has complied with ■ PROD 4 (see also ■ PROD 4.4.2G). ■ PROD 4.4 includes guidance based on the RPPD which firms subject to ■ PROD 4 should apply.
1.5 Application of PROD 5

General: Who? What?

1.5.1 R PROD 5 applies to a firm which:

(1) offers to sell an extended warranty to a customer; or

(2) refers, invites or induces a customer to obtain an extended warranty from a person connected to the firm;

in connection with the entering into of a rent-to-own agreement with the firm.

1.5.2 G A person connected to the firm includes someone who has a relevant business relationship with the firm.

Where?

1.5.3 R PROD 5 applies to a firm with respect to activities carried on from an establishment maintained by it, or its appointed representative, in the United Kingdom.

EEA territorial scope rule: compatibility with European law

1.5.4 R (1) The territorial scope of PROD 5 is modified to the extent necessary to make it compatible with European law (see PROD 1.5.5G to PROD 1.5.7G for guidance on this).

(2) This rule overrides every other rule in PROD 5.

Effects of the EEA territorial scope rule

1.5.5 G The guidance in paragraph 2 of Part 4 of ICOBS 1 Annex 1 applies equally to the rules in PROD 5.
IDD, Solvency II, DMD: effect on territorial scope

1.5.6 G The guidance on the IDD, Solvency II and Distance Marketing Directive in ▪ ICOBS 1 Annex 1 in relation to ▪ ICOBS 6A.1.4R applies equally to ▪ PROD 5.1.1R (to the extent that the extended warranty is a contract of insurance).

Electronic Commerce Directive: effect on territorial scope

1.5.7 G The guidance on the Electronic Commerce Directive in ▪ ICOBS 1 Annex 1, Part 4, paragraph 8 applies equally in relation to the rules in ▪ PROD 5.
Chapter 2

Statement of policy with respect to the making of temporary product intervention rules
2.1 Purpose

2.1.1 This chapter explains the FCA’s policy with respect to the making of temporary product intervention rules under sections 137D and 138M of the Act. This statement of policy replaces the “Statement of Policy for making temporary product intervention rules” published in Policy Statement PS13/03 (see https://www.fca.org.uk/publication/policy/fsa-ps13-03.pdf).

[Note: see section 138N of the Act]

2.1.2 Product intervention rules are rules made under section 137D of the Act which apply to specific products (or types of products), product features or marketing practices relating to specific products.

2.1.3 Product intervention rules may be made without consultation under section 138M of the Act but are limited to a maximum duration of 12 months and are referred to as “temporary product intervention rules”.
2.2 General rule making and product intervention rules

2.2.1 The Act empowers the FCA to make general rules as appear necessary or expedient for the purpose of advancing one or more of its operational objectives.

[Note: see section 137A of the Act]

2.2.2 The Act also provides that the FCA may use its general rule-making power to make product intervention rules prohibiting authorised persons from, among other things, entering into specified agreements (section 137D of the Act). These rules may be made to advance:

(1) the consumer protection objective; or

(2) the competition objective; or

(3) the market integrity objective.

2.2.3 Section 137D(2) of the Act sets out that the FCA may prohibit authorised persons from:

(1) entering into specified agreements with any person or specified person (specified person means a person who meets the description specified by FCA rules);

(2) entering into specified agreements with any person or specified person unless requirements specified in the rules have been satisfied;

(3) doing anything that would or might result in the entering into of specified agreements by persons or specified persons, or the holding by them of a beneficial or other kind of economic interest in specified agreements; and

(4) doing anything within paragraph (3) unless requirements specified in the rules have been satisfied.

2.2.4 Section 137D of the Act makes it clear that a range of options would be available to us in making rules prohibiting authorised persons from entering into specified agreements.
The extent of the rules which are made will generally depend on the type of intervention deemed necessary to address the issues identified, having regard to whether the intervention would be a proportionate response to the perceived risk to consumers, competition issues or market integrity issues.

Rules may include:

1. requiring certain product features to be included, excluded or changed; or
2. requiring amendments to promotional materials; or
3. the imposition of restrictions on sales or marketing of the product; or
4. in more serious cases, a ban on sales or marketing of a product in relation to all or some types of client.

Where the product is provided by a business outside of the UK, rules may be made targeting regulated activities by authorised persons in the UK that would lead to a specified agreement being formed.

[Note: see sections 137D(2)(c) and (d) of the Act]
2.3 Agreements made in breach of product intervention rules

2.3.1 In relation to agreements entered into in breach of product intervention rules, section 137D(7) sets out that the rules may:

(1) provide for a relevant agreement or obligation to be unenforceable against any person or specified person;

(2) provide for the recovery of any money or other property paid or transferred under a relevant agreement or obligation by any person or specified person; and

(3) provide for the payment of compensation for any loss sustained by any person or specified person as a result of paying or transferring any money or other property under a relevant agreement or obligation.

2.3.2 Where a rule provides for a relevant agreement or obligation to be unenforceable, the relevant agreement or obligation would only be unenforceable if the sale of the product was made after the introduction of the rules and there was a contravention of those rules. Clients with products bought after the introduction of rules incorporating unenforceability provisions would generally need to seek redress through the usual channels of complaints to the firm and to the Financial Ombudsman Service, or legal action against the firm.

2.3.3 Arrangements made before the introduction of the rules would not be affected by the unenforceability and compensation provisions. Clients holding contracts made before these rules were in place would still be able to seek redress through the usual channels of complaints to the firm and to the Financial Ombudsman Service or legal action against the relevant firm. These clients would need to establish their claim to redress in the usual way, for example by demonstrating that the advice they received was unsuitable, or that they bought the product after receiving a misleading financial promotion.
2.4 Temporal product intervention rules

2.4.1 Normally the FCA must consult the public before making any rules. However, the Act allows a general exemption in section 138L where the FCA considers that the delay involved in complying with the requirement to consult would be prejudicial to the interests of consumers.

2.4.2 There is also a specific exemption to the consultation requirement in relation to making temporary product intervention rules (section 138M of the Act). The FCA may make temporary product intervention rules without consultation if it considers that it is necessary or expedient not to comply with such a requirement to advance:

1. the consumer protection objective, or
2. the competition objective, or
3. the market integrity objective.

2.4.3 The FCA’s discretion to act under section 138M is therefore wider than under section 138L.

2.4.4 Decisions to make any rules, including temporary product intervention rules, will be taken by the FCA Board. In doing so, the FCA Board will have regard to all the available, relevant evidence, as well as the impact of the measure to be introduced by the rule.

2.4.5 The FCA Board will consider whether the evidence is sufficient to support the proposed measure and whether the measure is a proportionate response to the issue identified.

2.4.6 In publishing temporary product intervention rules the FCA will also publish the rationale for these rules.
2.5 Factors the FCA will consider when making temporary product intervention rules

2.5.1 In general terms the FCA will consider a product intervention rule where we identify a risk of consumer detriment, a threat to market integrity or ineffective competition arising from a particular product, type of product, or practices associated with a particular product or type of product.

2.5.2 In deciding whether the rule should be made as a temporary product intervention rule, the FCA’s main consideration will generally be whether prompt action is deemed necessary in seeking to reduce or prevent consumer detriment or a threat to market integrity or ineffective competition arising from that product, type of product or practices.
2.6 General considerations for product intervention rules

2.6.1 Together with the considerations in PROD 2.5, when making temporary or permanent product intervention rules, the FCA will have regard to the regulatory principles set out in section 3B of the Act, (see PROD 2.9).

2.6.2 The FCA will also take into account general considerations that include, but are not limited to, whether the proposed rules are:

1. an appropriate and effective means of addressing actual or potential consumer detriment associated with a particular product or group of products;
2. a proportionate and deliverable means of addressing actual or potential detriment;
3. compatible with the FCA’s duty to promote effective competition in the interests of consumers (section 1B(4) of the Act);
4. supported by sufficient and appropriate evidence;
5. transparent in their aim and operation;
6. likely to be beneficial for clients when taken as a whole; and
7. compatible (where relevant) with other applicable law, for example EU law.

2.6.3 In accordance with the Equality Act 2010, the FCA will have due regard to the need to:

1. eliminate discrimination, harassment, victimisation and any other conduct that is prohibited by or under the Equality Act 2010;
2. advance equality of opportunity between persons who share a relevant protected characteristic and persons who do not share it; and
3. foster good relations between persons who share a relevant protected characteristic and persons who do not share it;

when making temporary or permanent product intervention rules.
2.7 Contextual considerations for product intervention rules

2.7.1 When the FCA is considering whether to make temporary or permanent product intervention rules in response to an identified issue with a product, the following factors may be taken into account:

1. The potential scale of detriment in the market. Issues involving products with a large or potentially large client base are more likely to require product intervention.

2. The potential scale of detriment to individual clients. Issues that may lead to high detriment for individual clients are more likely to require product intervention.

3. The social context. Issues that may lead to detriment for particular groups of clients (such as, in particular, vulnerable client groups) are more likely to require product intervention.

4. The market context. Market mechanisms such as information disclosure and competition do not always work to protect consumers.

5. Possible unintended consequences. Whether the use of product intervention rules or the timing of the intervention would in itself create undue risk of further consumer detriment, including harm to existing clients and in the market (although this will not necessarily comprise a full cost benefit analysis).
2.8 Competition considerations for temporary product intervention rules

2.8.1 When making a temporary or permanent product intervention rule, the FCA will seek to promote effective competition in the interests of consumers where doing so is compatible with its consumer protection objective or integrity objective.

2.8.2 In accordance with section 1E of the Act the FCA also has a competition objective and may make rules, including temporary product intervention rules, specifically to advance competition.

2.8.3 Relevant competition-related considerations for the FCA in the context of temporary or permanent product intervention rules are likely to include:

1. Whether there is reasonable scope for the rules under consideration to promote effective competition in the interests of consumers, for instance by addressing consumer behaviours that impair their ability to benefit from competition, by reducing information asymmetries or by correcting misaligned incentives.

2. Whether the rule under consideration may have a negative impact on competition factors such as product innovation and barriers to entry for new market participants.

3. Whether any negative impact on competition factors is proportionate, having regard to the aims of the rule under consideration.

4. Whether alternative solutions may deliver the same intended outcome while having a more positive impact on competition.

5. The overall effect of a proposed rule upon the operation of effective competition in the market for financial services, having regard to the interests of consumers.
2.9 Regulatory principles

2.9.1 The FCA will have regard to the regulatory principles set out in section 3B of the Act when making temporary product intervention rules.

2.9.2 As part of the FCA's consideration of issues including the desirability of facilitating innovation, we will consider the potential deterrent effect on entry to the market and innovation when making temporary product intervention rules against the potential for reducing anticipated consumer detriment.
2.10 Process for making temporary product intervention rules

2.10.1 Once initial proposals have been discussed, a paper will be prepared at working group level for a committee (the Committee) with appropriate authority to propose temporary product intervention rules to the FCA Board.

2.10.2 The Committee will either endorse the proposals and recommend that they are taken to the Board, or suggest rethinking or amending the proposals and coming back at a later date. A decision may be taken to use a different regulatory tool, or not to proceed.

2.10.3 If the Committee decides that the proposals should go to the Board, the paper will be taken to the next available scheduled Board meeting, unless the matter is of great importance or there is an emergency, in which case the Board may convene specifically to consider the issue.

2.10.4 If the Board makes a decision to act on the policy proposals the FCA will publish the temporary product intervention rules on its website and take the necessary follow-up actions.
2.11 Consulting the panels

2.11.1 The FCA will generally seek the views of the Financial Services Practitioner Panel, the Smaller Businesses Practitioner Panel and the Financial Services Consumer Panel during the process for making temporary product intervention rules if there is sufficient time to do so.
2.12 Consulting the PRA

2.12.1 Before any proposed product intervention *rules* are made (whether temporary or not) the *FCA* will consult the *PRA*. 
2.13 Communication, publication and post-implementation review of temporary product intervention rules

2.13.1 Before making a temporary product intervention rule, the Committee will consider how affected firms and clients are to be informed of the rule in good time.

2.13.2 The FCA will publish a statement on its website explaining why it is introducing the rule. The FCA may choose to invite feedback, but this will not amount to a consultation exercise.

2.13.3 The FCA may choose to review a temporary product intervention rule during the term for which the rule is in force. Such a review will generally depend on the perceived risk the rule seeks to mitigate. These reviews may be informed by market monitoring and feedback from stakeholders, including product manufacturers, distributors and clients.

2.13.4 Where the FCA perceives potential uncertainty about how the rule operates, it may consider publishing guidance.

2.13.5 Reviews are likely to consider whether a rule is functioning as intended, including whether:

(1) there have been any breaches of the rule; or

(2) there are any unintended consequences, such as an impact on products that were not intended to be caught by the rule; or

(3) there is evidence suggesting firms are avoiding or seeking to avoid the rule rather than complying with it, for instance where new products enter the market or new features are added to existing products that expose clients to the same or similar potential detriment; or,

(4) new evidence demonstrates that the rule is not necessary or detriment is unlikely.
2.13.6 As a result of these reviews, where necessary, the FCA may:

(1) revoke a temporary product intervention rule; or

(2) amend the rule, for example where a rule specifies certain criteria under which the sale of a product may continue, change these criteria.

2.13.7 Subsequent changes to a temporary product intervention rule will be communicated by issuing a new statement containing the revised rule and the rationale for the changes. Such changes will not extend the lifespan of the temporary product intervention rule.

2.13.8 However, the FCA may consult on a new rule to replace the temporary product intervention rule from the date on which the temporary product intervention rule ceases to have effect. This exercise would be subject to the FCA’s standard rule-making procedure including market failure analysis, cost benefit analysis and consultation to which all stakeholders, including manufacturers, distributors and clients would be invited to reply.
2.14 Revocation or replacement of rules

2.14.1 When making temporary product intervention rules the FCA will state the duration of the rule and the date from which it will be effective. Temporary product intervention rules will have a maximum duration of 12 months from when the rule is made, but the FCA may decide on a shorter duration for a rule.

2.14.2 The FCA may review or revoke temporary product intervention rules at any time before the end of the period for which they apply.

2.14.3 Rules may be revoked or amended for a number of reasons, including but not limited to:

   (1) new rules are introduced on a permanent basis following a consultation exercise; or

   (2) industry initiatives are developed that specify sufficient minimum standards to address the sources of consumer detriment; or

   (3) further evidence is submitted that demonstrates that consumer detriment will not occur; or

   (4) demand for, or supply of, the relevant product disappears and is deemed unlikely to return; or

   (5) the FCA identifies unforeseen negative effects of the rule which outweigh any positive impact upon consumer protection.

2.14.4 Where temporary product intervention rules have been made, the FCA may not make further temporary product intervention rules containing the same, or substantially the same, provisions within 12 months beginning on the day on which the limited duration of the initial rules ends (whether or not the rules were revoked early). This period does not apply to rules that are not temporary product intervention rules, (i.e. rules which had been made subject to consultation, whether or not of set duration).
Chapter 3

Product governance: MiFID
3.1 General

[Note: ESMA has also issued guidelines under article 16(1) of the ESMA Regulation covering: “MiFID II product governance requirements”, dated 5th February 2018. See https://www.esma.europa.eu/sites/default/files/library/esma35-43-620_guidelines_on_mifid_ii_product_governance_requirements_0.pdf.]

Interpretation: financial instruments and structured products

For the purposes of PROD 3, references to financial instruments include structured deposits.

3.1.1 □ For the purposes of PROD 3, references to financial instruments include structured deposits.

Proportionate application of rules

3.1.2 □ (1) A firm must, when manufacturing financial instruments or deciding on the range of financial instruments and investment services it intends to distribute to clients, comply, in a way that is appropriate and proportionate, with the requirements set out in this chapter.

(2) In complying with these requirements, a firm must take into account:

(a) the nature of the financial instrument or investment service; and

(b) the target market for the financial instrument.

[Note: articles 9(1) and 10(1) of the MiFID Delegated Directive]

3.1.3 □ A proportionate application of the requirements in this chapter may mean that complying with the rules could be relatively simple for simple financial instruments distributed on an execution-only transaction basis where such financial instruments would be compatible with the needs and characteristics of the mass retail market.
3.2 Manufacture of products

General

3.2.1 A manufacturer must:

(1) ensure that the financial instruments it manufactures are designed to meet the needs of an identified target market of end clients within the relevant category of clients (see COBS 3 for client categories);

(2) ensure that the strategy for distribution of the financial instruments is compatible with the identified target market; and

(3) take reasonable steps to ensure that the financial instrument is distributed to the identified target market.

[Note: article 24(2) of MiFID]

3.2.2 Consideration of target market factors should permeate all aspects of product development and distribution, as well as ensuring the selection of appropriate distribution channels and the promotion of the financial instruments are accompanied by sufficient and correct information.

Product governance arrangements

3.2.3 A manufacturer must maintain, operate and review a process for the approval of:

(1) each financial instrument, and

(2) significant adaptations of existing financial instruments,

in each case before they are marketed or distributed to clients.

[Note: article 16(3) of MiFID]

3.2.4 For each financial instrument the product approval process must:

(1) specify an identified target market of end clients within the relevant category of clients (see COBS 3 for client categories);

(2) ensure that all relevant risks to the identified target market are assessed; and
(3) ensure that the intended distribution strategy is consistent with the identified target market.

[Note: article 16(3) of MiFID]

3.2.5 When designing financial instruments, a firm should have in place systems and controls to manage adequately the risks posed by financial instrument design.

Manufacture by more than one firm

3.2.6 Where firms collaborate to manufacture a financial instrument, only one target market needs to be identified.

[Note: article 9(9) of the MiFID Delegated Directive]

3.2.7 Where firms collaborate, including with entities which are not authorised and supervised in accordance with MiFID or third country investment firms, to create, develop, issue and/or design a financial instrument, they must outline their mutual responsibilities in a written agreement.

[Note: article 9(8) of the MiFID Delegated Directive]

Target market

3.2.8 Manufacturers must identify the potential target market for each financial instrument at a sufficiently granular level and must:

1. specify the type or types of client for whose needs, characteristics and objectives the financial instrument is compatible; and
2. identify any group or groups of client for whose needs, characteristics and objectives the financial instrument is not compatible.

[Note: article 9(9) of the MiFID Delegated Directive]

3.2.9 The level of granularity of the target market and the criteria used to define the target market and determine the appropriate distribution strategy should be relevant for the financial instrument and should make it possible to assess which clients fall within the target market. For simpler, more common financial instruments, the target market could be identified with less detail while for more complicated financial instruments such as bail-inable instruments or less common financial instruments, the target market should be identified with more detail.

[Note: recital 19 of the MiFID Delegated Directive]

3.2.10 Manufacturers must determine for each financial instrument they manufacture, whether it meets the identified needs, characteristics and objectives of the target market, and in doing so must include an examination of the following elements:

1. whether the financial instrument’s risk/reward profile is consistent with the target market; and
(2) whether the design of the *financial instrument* is driven by features that benefit the *client* and not by a business model which relies on poor *client* outcomes to be profitable.

[Note: article 9(11) of the *MiFID Delegated Directive*]

3.2.11 Manufacturers of financial instruments that are distributed through other firms must determine the needs and characteristics of the *clients* for whom the product is compatible based on:

1. their theoretical knowledge of, and past experience with, the *financial instrument* or similar *financial instruments*;
2. the financial markets, and
3. the needs, characteristics and objectives of potential *end clients*.

[Note: article 9(9) of the *MiFID Delegated Directive*]

Product testing

3.2.12 Manufacturers must undertake a scenario analysis of their *financial instruments* to assess:

1. the risks of poor outcomes for *end clients* posed by the *financial instrument*; and
2. in which circumstances those poor outcomes may occur.

[Note: article 9(10) *MiFID Delegated Directive*]

3.2.13 In conducting the scenario analysis manufacturers must assess their *financial instruments* under negative conditions covering what would happen if, for example:

1. the market environment deteriorated; or
2. the *manufacturer* or a third party involved in manufacturing and/or the functioning of the *financial instrument* experiences financial difficulties or other counterparty risk materialises; or
3. the *financial instrument* fails to become commercially viable; or
4. demand for the *financial instrument* is much higher than anticipated, putting a strain on the *firm’s* resources and/or on the market of the underlying *financial instrument*.

[Note: article 9(10) *MiFID Delegated Directive*]

3.2.14 Manufacturers must consider the charging structure proposed for each *financial instrument*, including examination of the following:

1. whether the *financial instrument’s* costs and charges are compatible with the needs, objectives and characteristics of the target market;
(2) whether the charges undermine the financial instrument’s return expectations, such as where the costs or charges equal, exceed or remove almost all the expected tax advantages linked to a financial instrument; and

(3) whether the charging structure of the financial instrument is appropriately transparent for the target market, such as that it does not disguise charges or is too complex to understand.

[Note: article 9(12) of the MiFID Delegated Directive]

3.2.15 Manufacturers must consider whether the financial instrument may represent a threat to the orderly functioning, or to the stability, of financial markets before deciding to proceed with the launch of the financial instrument.

[Note: article 9(4) of the MiFID Delegated Directive]

Information disclosure to distributors

3.2.16 A manufacturer must make available to any distributor of that financial instrument:

(1) all appropriate information on the financial instrument;

(2) all appropriate information on the product approval process;

(3) the identified target market of the financial instrument, including information about the target market assessment undertaken;

(4) information about the appropriate channels for distribution of the financial instrument;

and must ensure that the information is of an adequate standard to enable distributors to understand and recommend or sell the financial instrument properly.

[Note: article 16(3) of MiFID II and 9(13) of the MiFID Delegated Directive]

3.2.17 When providing information to distributors, a manufacturer should make it clear if that information is not intended for end client use.

3.2.18 Manufacturers may consider, for example, with regard to each distribution channel or type of distributor what information distributors of that type already have, their likely level of knowledge and understanding, their information needs and what form or medium would best meet those needs (which could include discussions, written material or training as appropriate).

Review of financial instruments

3.2.19 (1) A manufacturer must regularly review the financial instruments it manufactures taking into account any event that could materially affect the potential risk to the identified target market.

(2) In doing so, a manufacturer must assess for each financial instrument at least the following:
(a) whether the financial instrument remains consistent with the needs, characteristics and objectives of the identified target market;
(b) whether the intended distribution strategy remains appropriate;
(c) whether the financial instrument is being distributed to the target market; and
(d) whether the financial instrument is reaching clients for whose needs, characteristics and objectives the financial instrument is not compatible.

[Note: article 16(3) of MiFID II and article 9(14) of the MiFID Delegated Directive]

3.2.20 In carrying out the reviews in PROD 3.2.19 manufacturers should collect and analyse appropriate management information to detect patterns in distribution as compared with the planned target market in order to assess the performance of the distribution channels through which a financial instrument is being distributed.

3.2.21 (1) When reviewing the financial instruments it manufactures, a firm should communicate to the end client contractual “breakpoints” such as the end of a long tie-in period that may have a material impact on the end client that the end client cannot reasonably be expected to recall or know about already.

(2) If the manufacturer does not know the identity of the end client, it should communicate any contractual breakpoints to the distributor.

3.2.22 Manufacturers must:

(1) review financial instruments prior to any further issue or re-launch if they are aware of any event that could materially affect the potential risk to clients; and

(2) identify crucial events that would affect the potential risk or return expectations of the financial instrument.

3.2.23 Crucial events that would affect the potential risk or return expectations of the financial instrument include:

(1) the crossing of a threshold that will affect the return profile of the financial instrument; or

(2) the solvency of certain issuers whose securities and guarantees may impact the performance of the financial instrument.

3.2.24 When a crucial event affecting the potential risk or return expectation of the financial instrument occurs, a manufacturer must take appropriate action, which may consist of:

(1) the provision of any relevant information on the event and its consequences on the financial instrument to the clients or distributors
of the financial instrument if the manufacturer does not offer or sell the financial instrument directly to the clients;

(2) changing the product approval process;

(3) stopping further issuance of the financial instrument;

(4) changing the financial instrument to avoid unfair contract terms;

(5) considering whether the sales channels through which the financial instrument is sold are appropriate where the manufacturer becomes aware that the financial instrument is not being sold as envisaged;

(6) contacting the distributor to discuss a modification of the distribution process;

(7) terminating the relationship with the distributor; or

(8) informing the relevant competent authority.

3.2.25 Manufacturers must review financial instruments at regular intervals to assess whether they function as intended.

3.2.26 Manufacturers must determine how regularly to review their financial instruments based on relevant factors including factors linked to the complexity or the innovative nature of the investment strategies pursued.

[Note: article 9(15) of the MiFID Delegated Directive]

Conflicts of interest

3.2.27 Manufacturers must establish, implement and maintain procedures and measures to ensure the manufacture of financial instruments complies with the requirements on proper management of conflicts of interest (see SYSC 10.1.7R), including remuneration.

3.2.28 Manufacturers must ensure that the design of each financial instrument, including its features, does not:

(1) adversely affect end clients; or

(2) lead to problems with market integrity by enabling the firm to mitigate and/or dispose of its own risks or exposure to the underlying assets of the product where the firm already holds the underlying assets on own account.

[Note: article 9(2) of the MiFID Delegated Directive]

3.2.29 Each time a financial instrument is manufactured manufacturers must analyse potential conflicts of interests.
In analysing potential conflicts of interest manufacturers must assess whether the financial instrument creates a situation where end clients may be adversely affected if end clients take:

(1) an exposure opposite to the one previously held by the manufacturer itself; or

(2) an exposure opposite to the one that the manufacturer wants to hold after the sale of the product.

[Note: article 9(3) of the MiFID Delegated Directive]

Oversight and training requirements

Manufacturers must ensure that their management bodies have effective control over their product governance process.

The development and periodic review of product governance arrangements must be monitored by the person allocated the compliance oversight function of a firm in order to detect any risk of failure by the manufacturer to comply with applicable provisions of PROD.

[Note: article 9(6) and article 9(7) of the MiFID Delegated Directive]

All relevant staff involved in the manufacturing of financial instruments must possess the necessary expertise to understand the characteristics and risks of the financial instruments they intend to manufacture.

[Note: article 9(5) of the MiFID Delegated Directive]

Firms should have regard to SYSC 5.1, and in particular SYSC 5.1.5AB R, when considering whether their relevant staff have the necessary expertise.

Compliance reports

Compliance reports to the management body must include information about the financial instruments that the firm has manufactured, including information on the distribution strategy.

Manufacturers must make the compliance reports available to their competent authority on request.

[Note: article 9(6) MiFID Delegated Directive]
3.3 Distribution of products and investment services

General

3.3.1 R A distributor must:

(1) understand the financial instruments it distributes to clients;

(2) assess the compatibility of the financial instruments with the needs of the clients to whom it distributes investment services, taking into account the manufacturer’s identified target market of end clients; and

(3) ensure that financial instruments are distributed only when this is in the best interests of the client (see □ COBS 2.1.1R(1)).

[Note: article 24(2) of MiFID]

3.3.2 G A distributor should consider what impact the selection of a given manufacturer could have on the end client in terms of charges or the financial strength of the manufacturer, or possibly, where information is available to the distributor, how efficiently and reliably the manufacturer will deal with the distributor or end client at the point of sale (or subsequently, such as when queries/complaints arise, claims are made, or a financial instrument reaches maturity).

Obtaining information from manufacturers

3.3.3 R Distributors must obtain from MiFID manufacturers information to gain the necessary understanding and knowledge of the financial instruments they intend to distribute in order to ensure that the financial instruments will be distributed in accordance with the needs, characteristics and objectives of the target market.

[Note: article 16(3) MiFID and article 10(2) MiFID Delegated Directive]

3.3.4 G In ensuring that they have obtained sufficient information about the financial instruments they distribute and in ensuring they understand the financial instruments or investment services distributed, distributors:

(1) should consider whether they understand the materials provided by the manufacturer or distributor earlier in the sales chain;
(2) should ask the manufacturer to supply additional information or training where this seems necessary to understand the financial instrument or investment service adequately;

(3) should not distribute the financial instrument or investment service if they do not understand it sufficiently; and

(4) when providing information to another distributor in a distribution chain, should consider how the further distributor will use the information, such as whether it will be given to end clients. Firms should consider what information the further distributor requires and the likely level of knowledge and understanding of the further distributor and what medium may suit it best for the transmission of information.

Distributing financial instruments manufactured by non-MiFID firms, including third country firms

3.3.5 Distributors must take all reasonable steps to comply with PROD 3.3 when distributing financial instruments manufactured by any firm to which MiFID manufacturer product governance requirements (PROD 3.2 or equivalent requirements of another EEA State) do not apply.

(2) As part of this, distributors must put in place effective arrangements to ensure that they obtain sufficient, adequate and reliable information from the manufacturer about the financial instruments to ensure that they will be distributed in accordance with the characteristics, objectives and needs of the target market.

(3) This rule applies to financial instruments sold on either the primary or secondary market.

3.3.6 The obligation to obtain adequate and reliable information applies proportionately depending on:

(1) the degree to which publicly available information is obtainable; and

(2) the complexity of the financial instrument.

[Note: articles 10(1) and 10(2) of the MiFID Delegated Directive]

3.3.7 Where information relevant to the obligation in PROD 3.3.5R is not publicly available, distributors must take all reasonable steps to obtain such relevant information from the manufacturer or its agent.

3.3.8 Acceptable publicly available information is information which is clear, reliable and produced to meet regulatory requirements, such as disclosure requirements under the transparency rules or the Prospectus Regulation.

[Note: article 10(2) of the MiFID Delegated Directive]
**Target market and distribution strategy**

**3.3.9** Distributors must determine the target market for the respective financial instrument, even if the target market was not defined by the manufacturer.  

[Note: article 10(1) of the MiFID Delegated Directive]

**3.3.10** Distributors must identify the target market and their distribution strategy using:

1. the information obtained from manufacturers; and
2. information they have on their own clients.

**3.3.11** In identifying the target market and creating a distribution strategy, distributors should consider:

1. the nature of the financial instruments to be offered or recommended and how they fit with end clients’ needs and risk appetite;
2. the impact of charges on end clients;
3. the financial strength of the manufacturer; and
4. where information is available on the manufacturer’s processes, how efficiently and reliably the manufacturer will deal with the end client at the point of sale or subsequently, such as when complaints arise, claims are made or the financial instrument reaches maturity.

**3.3.12** The target market identified by distributers for each financial instrument should be identified at a sufficiently granular level.

**3.3.13** Where a distributor is part of a distribution chain, the information referred to in PROD 3.3.10R(2) should include information on the intended end client.

**3.3.14** Where a firm acts both as a manufacturer and a distributor, only one target market assessment is required.  

[Note: article 10(2) of the MiFID Delegated Directive]

**3.3.15** (1) Distributors must have in place adequate product governance arrangements to ensure that:

- the financial instruments and investment services they intend to distribute are compatible with the needs, characteristics and objectives of the identified target market; and
- the intended distribution strategy is consistent with the identified target market.

(2) Distributors must appropriately identify and assess the circumstances and needs of the clients they intend to focus on to ensure that their...
clients’ interests are not compromised as a result of commercial or funding pressures.

(3) Distributors must identify any groups of end clients for whose needs, characteristics and objectives the financial instrument or investment service is not compatible.

[Note: article 10(2) of the MiFID Delegated Directive]

3.3.16 R Distributors must periodically review their product governance arrangements under ■ PROD 3.3.15R and must take appropriate actions where necessary to ensure they remain robust and fit for their purpose.

[Note: article 16(3) of MiFID and article 10(4) of the MiFID Delegated Directive]

3.3.17 G In the design of investment services, to help clients make an informed investment decision, firms should consider the support clients need before they reach the product selection part of the process.

3.3.18 R Distributors must have in place procedures and measures to ensure that when deciding the range of financial instruments and investment services to be distributed, and the target market, all applicable rules are complied with, including but not limited to:

   (1) disclosure (see ■ COBS 4 and ■ COBS 14.3A);
   (2) suitability (see ■ COBS 9A);
   (3) appropriateness (see ■ COBS 10A);
   (4) inducements (see ■ COBS 2.3A); and
   (5) conflicts of interest (see ■ SYSC 10.1).

3.3.19 G Distributors should take particular care to ensure compliance with ■ PROD 3.3.18R when they intend to distribute new financial instruments or there are variations to the investment services they provide.

[Note: article 10(3) of the MiFID Delegated Directive]

Oversight and training requirements

3.3.20 R The development and periodic review of product governance arrangements must be monitored by the person allocated the compliance oversight function of a firm in order to detect any risk of failure by the distributor to comply with applicable provisions of PROD.

[Note: article 10(6) of the MiFID Delegated Directive]

3.3.21 R The management body of a distributor must have effective control over the firm’s product governance process to determine:
(1) the range of financial instruments the firm offers or recommends; and
(2) the investment services provided to the respective target markets.

[Note: article 10(8) of the MiFID Delegated Directive]

3.3.22 All relevant staff must possess the necessary expertise to understand:

(1) the characteristics and risks of the financial instruments that the firm intends to distribute;
(2) the investment services provided by the firm; and
(3) the needs, characteristics and objectives of the identified target market.

[Note: article 10(7) of the MiFID Delegated Directive]

3.3.23 Firms should have regard to SYSC 5.1, and in particular SYSC 5.1.5AB R, when considering whether their relevant staff have the necessary expertise.

Compliance reports

3.3.24 Compliance reports to the management body must include information about the financial instruments distributed by the firm and the investment services provided.

3.3.25 A distributor shall make the compliance reports available to competent authorities on request.

[Note: article 10(8) of the MiFID Delegated Directive]

Post-sale review

3.3.26 Distributors must regularly review the financial instruments they distribute and the investment services they provide, taking into account any event that could materially affect the potential risk to the identified target market.

3.3.27 In carrying out the review in PROD 3.3.26R, distributors must assess at least:

(1) whether the financial instrument or investment service remains consistent with the needs, characteristics and objectives of the identified target market; and
(2) whether the intended distribution strategy remains appropriate.

3.3.28 If a distributor becomes aware that it has wrongly identified the target market for a specific financial instrument or investment service, or the financial instrument or investment service no longer meets the circumstances of the identified target market, it must take appropriate steps, including at least:
(1) reconsidering the target market; and/or
(2) updating its product governance arrangements.

A distributor may need to take action under ■ PROD 3.3.28R in circumstances where the financial instrument becomes very illiquid or very volatile due to market changes.

[Note: article 16(3) of MiFID and article 10(5) of the MiFID Delegated Directive]

### Information sharing

To support the reviews carried out by manufacturers under ■ PROD 3.2.19R to ■ PROD 3.2.26R, a distributor must provide to the manufacturer of each financial instrument it distributes:

(1) information on sales; and
(2) where appropriate, information on the reviews carried out under ■ PROD 3.3.26R to ■ PROD 3.3.28R.

(1) Information on sales should include information on any sales made outside the target market.

(2) In complying with ■ PROD 3.3.30R it is not necessary to report every sale to the manufacturer. Distributors should provide the data necessary for the manufacturer to review the financial instrument and check that it remains consistent with the needs, characteristics and objectives of the target market defined by the manufacturer. Relevant information could include:

(a) summary information of the types of clients;
(b) a summary of complaints received; and
(c) responses from clients to questions suggested by the manufacturer for the purposes of obtaining feedback from a client sample.

(3) In determining when providing information on the reviews carried out under ■ PROD 3.3.26R to ■ PROD 3.3.28R is appropriate, a distributor should have regard to the requirements on the manufacturer in ■ PROD 3.2. Information on the reviews should be shared if the manufacturer requests it.

[Note: article 10(9) of and recital 20 to the MiFID Delegated Directive]

### Responsibilities in chains of distributors

(1) A firm which distributes financial instruments or investment services to end clients is responsible for ensuring that the obligations in this chapter are met in respect of any financial instrument or investment service it distributes to an end client.

(2) A firm which distributes financial instruments to clients which are not end clients must, in addition to complying with the rules in this
chapter, consider if they are also undertaking a *manufacturing* role and, if they are, also apply ■ PROD 3.2.

### 3.3.33

A *distributor* which *distributes financial instruments* to other *distributors* must:

1. ensure that relevant product information is passed from the *manufacturer* to the final *distributor* in the chain; and
2. if the *manufacturer* requires information on product sales in order to comply with its obligations under ■ PROD 3.2, enable them to obtain it.

**[Note: article 10(10) of the MiFID Delegated Directive]**
Chapter 4

Product governance: IDD
4.1 General

Other requirements under the IDD

This chapter does not affect the application of other requirements in the FCA Handbook applying to firms in relation to their insurance distribution activities including but not limited to:

1. disclosure (ICOBS 2.2, ICOBS 6.1, COBS 4 and COBS 14.2);
2. suitability (COBS 9 or COBS 9A);
3. appropriateness (COBS 10A);
4. identification and management of conflicts of interest (SYSC 10.1 for intermediaries or SYSC 3.3 for insurers); and
5. inducements (COBS 2.3A).

[Note: article 25(3) of the IDD]
4.2 Manufacture of insurance products

Product governance arrangements

4.2.1 A firm which manufactures any insurance product must maintain, operate and review a process for the approval of:

(1) each insurance product; and

(2) significant adaptations of an existing insurance product,

in each case before it is marketed or distributed to customers.

[Note: first subparagraph of article 25(1) of the IDD]

4.2.2 The product approval process referred to in PROD 4.2.1 must be proportionate and appropriate to the nature of the insurance product.

[Note: second subparagraph of article 25(1) of the IDD]

4.2.3 Manufacturers should take into account the following when considering whether the product approval process is proportionate and appropriate:

(1) the complexity of the insurance product;

(2) the degree to which publicly available information can be obtained;

(3) the nature of the insurance product and the risk of consumer detriment related to it;

(4) the characteristics of the target market; and

(5) the scale and complexity of the relevant business of the manufacturer or distributor.

[Note: recital 2 to the IDD POG Regulation]

4.2.4 For the purposes of PROD 4.2.2 proportionality means that the product approval process should be relatively simple for straightforward and non-complex products that are compatible with the needs and characteristics of the mass retail market. On the other hand, in the case of more complex products with a higher risk of consumer detriment more exacting measures should be required.

[Note: recital 2 to the IDD POG Regulation]
Product approval process

4.2.5 EU

4(1) Manufacturers shall maintain, operate and review a product approval process for newly developed insurance products and for significant adaptations of existing insurance products. That process shall contain measures and procedures for designing, monitoring, reviewing and distributing insurance products, as well as for corrective action for insurance products that are detrimental to customers. The measures and procedures shall be proportionate to the level of complexity and the risks related to the products as well as the nature, scale and complexity of the relevant business of the manufacturer.

[Note: article 4(1) of the IDD POG Regulation]

4.2.6 EU

4(2) The product approval process shall be set out in a written document ("product oversight and governance policy"), which shall be made available to the relevant staff.

[Note: article 4 (2) of the IDD POG Regulation]

4.2.7 EU

9 Relevant actions taken by manufacturers in relation to their product approval process shall be duly documented, kept for audit purposes and made available to the competent authorities upon request.

[Note: article 9 of the IDD POG Regulation]

4.2.8 EU

4(3) The product approval process shall

(a) ensure that the design of insurance products:
   (i) takes into account the objectives, interests and characteristics of customers;
   (ii) does not adversely affect customers;
   (iii) prevents or mitigates customer detriment;
(b) support a proper management of conflicts of interest.

[Note: article 4(3) of the IDD POG Regulation]

4.2.9 EU

4(4) The manufacturers' body or structure responsible for the manufacturing of insurance products shall:

(a) endorse and be ultimately responsible for establishing, implementing and reviewing the product approval process;
(b) continuously verify internal compliance with that process.

[Note: article 4(4) of the IDD POG Regulation]

4.2.10 EU

5(4) Manufacturers shall ensure that staff involved in designing and manufacturing insurance products has the necessary skills, knowledge and expertise to properly understand the insurance products sold and
the interests, objectives and characteristics of the customers belonging to the target market.

[Note: article 5(4) of the IDD POG Regulation]

4.2.11 EU 4(5)Manufacturers designating a third party to design products on their behalf shall remain fully responsible for compliance with the product approval process.

[Note: article 4(5) of the IDD POG Regulation]

4.2.12 EU 4(6)Manufacturers shall regularly review their product approval process to ensure that that process is still valid and up to date. They shall amend the product approval process where necessary.

[Note: article 4(6) of the IDD POG Regulation]

Manufacturer by more than one firm

3(4)An insurance intermediary and an insurance undertaking that are both manufacturers within the meaning of Article 2 of this Delegated Regulation, shall sign a written agreement which specifies their collaboration to comply with the requirements for manufacturers referred to in Article 25(1) of Directive (EU) 2016/97, the procedures through which they shall agree on the identification of the target market and their respective roles in the product approval process.

[Note: article 3(4) of the IDD POG Regulation]

In circumstances other than PROD 4.2.13EU, when firms collaborate to manufacture an insurance product, they must outline their mutual responsibilities in a written agreement.

Target market

For each insurance product the product approval process must:

(1) specify an identified target market;

(2) ensure that all relevant risks to the identified target market are assessed;

(3) ensure that the intended distribution strategy is consistent with the identified target market; and

(4) require the manufacturer to take reasonable steps to ensure that the insurance product is distributed to the identified target market.

[Note: third subparagraph of article 25(1) of the IDD]

5(1)The product approval process shall for each insurance product identify the target market and the group of compatible customers.
The target market shall be identified at a sufficiently granular level, taking into account the characteristics, risk profile, complexity and nature of the insurance product.

[Note: article 5(1) of the IDD POG Regulation]

4.2.17 EU 5(2) Manufacturers may, in particular with regard to insurance-based investment products, identify groups of customers for whose needs, characteristics and objectives the insurance product is generally not compatible.

[Note: article 5(2) of the IDD POG Regulation]

4.2.18 EU 5(3) Manufacturers shall only design and market insurance products that are compatible with the needs, characteristics and objectives of the customers belonging to the target market. When assessing whether an insurance product is compatible with a target market, manufacturers shall take into account the level of information available to the customers belonging to that target market and their financial literacy.

[Note: article 5(3) of the IDD POG Regulation]

4.2.19 G The identification of the target market by the manufacturer should be understood as describing a group of customers sharing common characteristics at an abstract and generalised level in order to enable the manufacturer to adapt the features of the product to the needs, characteristics and objectives of that group of customers.

4.2.20 G The identification of the target market should be distinguished from the individual assessment at the point of sale to determine whether a product meets the demands and needs and, where applicable, whether an insurance-based investment product is suitable or appropriate for the individual customer.

[Note: recital 5 to the IDD POG Regulation]

4.2.21 G The level of granularity of the target market and the criteria used to define the target market and determine the appropriate distribution strategy should be relevant for the product and should make it possible to assess which customers fall within the target market. For simpler, more common products, the target market should be identified with less detail while for more complicated products or less common products, the target market should be identified with more detail taking into account the increased risk of consumer detriment associated with such products.

[Note: recital 6 to the IDD POG Regulation]

Product testing

4.2.22 EU 6(1) Manufacturers shall test their insurance products appropriately, including scenario analyses where relevant, before bringing that product to the market or significantly adapting it, or in case the
target market has significantly changed. That product testing shall assess whether the insurance product over its lifetime meets the identified needs, objectives and characteristics of the target market. Manufacturers shall test their insurance products in a qualitative manner and, depending on the type and nature of the insurance product and the related risk of detriment to customers, quantitative manner.

[Note: article 6(1) of the IDD POG Regulation]

4.2.23 For the purposes of PROD 4.2.22EU, manufacturers should include assessments of the performance and risk/reward profile of their insurance product where appropriate.

[Note: recital 8 to the IDD POG Regulation]

4.2.24 Manufacturers shall not bring insurance products to the market if the results of the product testing show that the products do not meet the identified needs, objectives and characteristics of the target market.

[Note: article 6(2) of the IDD POG Regulation]

4.2.25 Manufacturers must consider the charging structure proposed for each insurance product, including examination of the following:

(1) whether the costs and charges of the insurance product are compatible with the needs, objectives and characteristics of the target market;

(2) where relevant, whether the charging structure of the insurance product is appropriately transparent for the target market, such as that it does not disguise charges or is too complex to understand; and

(3) where relevant, whether the charges undermine the return expectations of the insurance product, such as where the costs or charges equal, exceed or remove almost all the expected tax advantages linked to a life policy.

4.2.26 (1) PROD 4.2.25R does not affect the manufacturer’s freedom to set premiums.

(2) In relation to a non-investment insurance contract a firm should consider whether, as a result of the charging structure it has put in place, the overall cost for the customer is consistent with its obligations under the Principles and ICOBS.

(3) PROD 4.2.25R should be read in light of a firm’s wider obligations under the Handbook which impose specific restrictions or requirements around what costs and charges may be permissible. For example, the rules in COBS 20.2 govern what may be charged to a with-profits policy when considering its charging structure under PROD 4.2.25R.
### Distribution channels and information disclosure to distributors

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| 4.2.27 EU | 8(1) Manufacturers shall carefully select distribution channels that are appropriate for the target market, thereby taking into account the particular characteristics of the relevant insurance products.  

[Note: article 8(1) of the IDD POG Regulation] |

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| 4.2.28 G | To ensure appropriate information for customers, manufacturers should select distributors that have the necessary knowledge, expertise and competence to understand the features of an insurance product and the identified target market.  

[Note: recital 9 to the IDD POG Regulation] |

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| 4.2.29 R | A firm which manufactures an insurance product, must make available to a distributor:  

1. all appropriate information on the insurance product  
2. all appropriate information on the product approval process; and  
3. the identified target market of the insurance product.  

[Note: fifth subparagraph of article 25(1) of the IDD] |

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| 4.2.30 EU | 8(2) Manufacturers shall provide insurance distributors with all appropriate information on the insurance products, the identified target market and the suggested distribution strategy, including information on the main features and characteristics of the insurance products, their risks and costs, including implicit costs, and any circumstances which might cause a conflict of interest to the detriment of the customer. That information shall be clear, complete and up to date.  

[Note: article 8(2) of the IDD POG Regulation] |

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| 4.2.31 EU | 8(3) The information referred to in paragraph 2 shall enable the insurance distributors to:  

a) understand the insurance products;  

b) comprehend the identified target market for the insurance products;  

c) identify any customers for whom the insurance product is not compatible with their needs, characteristics and objectives;  

d) carry out distribution activities for the relevant insurance products in accordance with the best interests of their customers as prescribed in Article 17(1) of Directive (EU) 2016/97.  

[Note: article 8(3) of the IDD POG Regulation] |
A manufacturer must make available to any distributor information about the target market assessment.

The information made available under (1) must be of an adequate standard to enable distributors to:

- comprehend the identified target market for the insurance products; and
- be able to identify any customers for whom the insurance product is not compatible with their needs, characteristics and objectives.

A manufacturer is not required to disclose specific information objectively considered to be commercially sensitive if the information it does make available would still allow distributors to meet (2)(a) and (b).

**Monitoring and review of insurance products**

4.2.33 R A firm must understand the insurance products it offers or markets.

[Note: fourth subparagraph of article 25(1) of the IDD]

4.2.34 R A firm must regularly review the insurance products it offers or markets taking into account any event that could materially affect the potential risk to the identified target market. In doing so, the firm must assess at least the following:

1. whether the insurance product remains consistent with the needs of the identified target market; and
2. whether the intended distribution strategy remains appropriate.

[Note: fourth subparagraph of article 25(1) of the IDD]

4.2.35 EU Manufacturers shall continuously monitor and regularly review insurance products they have brought to the market, to identify events that could materially affect the main features, the risk coverage or the guarantees of those products. They shall assess whether the insurance products remain consistent with the needs, characteristics and objectives of the identified target market and whether those products are distributed to the target market or is reaching customers outside the target market.

[Note: article 7(1) of the IDD POG Regulation]

4.2.36 EU Manufacturers shall determine the appropriate intervals for the regular review of their insurance products, thereby taking into account the size, scale, contractual duration and complexity of those insurance products, their respective distribution channels, and any relevant external factors such as changes to the applicable legal rules, technological developments, or changes to the market situation.

[Note: article 7(2) of the IDD POG Regulation]
4.2.37 EU 7(3) Manufacturers that identify during the lifetime of an insurance product any circumstances related to the insurance product that may adversely affect the customer of that product shall take appropriate action to mitigate the situation and prevent further occurrences of the detrimental event. Manufacturers shall promptly inform concerned insurance distributors and customers about the remedial action taken.

[Note: article 7(3) of the IDD POG Regulation]

4.2.38 EU 8(4) Manufacturers shall take appropriate steps to monitor that insurance distributors act in accordance with the objectives of the manufacturers’ product approval process. They shall in particular verify on a regular basis whether the insurance products are distributed on the identified target market. That monitoring obligation shall not extend to the general regulatory requirements with which insurance distributors have to comply when carrying out insurance distribution activities for individual customers. The monitoring activities shall be reasonable, taking into consideration the characteristics and the legal framework of the respective distribution channels.

[Note: article 8(4) of the IDD POG Regulation]

4.2.39 EU 8(5) Manufacturers considering that the distribution of their insurance products is not in accordance with the objectives of their product approval process shall take appropriate remedial action.

[Note: article 8(5) of the IDD POG Regulation]
4.3 Distribution of insurance products

4.3.1 Where a firm distributes insurance products which it does not manufacture it must have in place adequate arrangements to obtain the information in [Note: sixth sub-paragraph of article 25(1) of the IDD]

4.3.2 Where a firm distributes insurance products which it does not manufacture, it must have in place adequate arrangements to understand:

(1) the characteristics of each insurance product; and

(2) the identified target market of each insurance product.

[Note: sixth sub-paragraph of article 25(1) of the IDD]

4.3.3 A distributor must take all reasonable steps to obtain the information in [Note: first sub-paragraph of article 10(1) of the IDD POG Regulation] when distributing insurance products manufactured by any person to which IDD manufacturer product governance requirements (PROD 4.2, equivalent requirements of another EEA State or directly applicable requirements of the IDD POG Regulation) do not apply.

4.3.4 To comply with PROD 4.3.2R, distributors should put in place effective arrangements to ensure that they obtain sufficient, adequate and reliable information from the manufacturer about the insurance products to ensure that they will be distributed in accordance with the characteristics, objectives and needs of the target market.

4.3.5 EU10(1)Insurance distributors shall have in place product distribution arrangements containing appropriate measures and procedures to obtain from the manufacturer all appropriate information on the insurance products they intend to offer to their customers and to fully comprehend those insurance products, taking into account the level of complexity and the risks related to the products as well as the nature, scale and complexity of the relevant business of the distributor.

[Note: first sub-paragraph of article 10(1) of the IDD POG Regulation]

4.3.6 EU10(2)The product distribution arrangements shall:

(a) aim to prevent and mitigate customer detriment;
(b)support a proper management of conflicts of interest;
(c)ensure that the objectives, interests and characteristics of customers are duly taken into account.

[Note: article 10(2) of the IDD POG Regulation]

10(3) The product distribution arrangements shall ensure that the insurance distributors obtain from the manufacturer the information to be communicated under Article 8(2).

[Note: article 10(3) of the IDD POG Regulation]

10(4) Any specific distribution strategy set up or applied by insurance distributors shall be in accordance with the distribution strategy set up and the target market identified by the manufacturer.

[Note: article 10(4) of the IDD POG Regulation]

10(5) The insurance distributors' body or structure responsible for insurance distribution shall endorse and be ultimately responsible for establishing, implementing and reviewing the product distribution arrangements and continuously verify internal compliance with those arrangements.

[Note: article 10(5) of the IDD POG Regulation]

10(6) Insurance distributors shall regularly review their product distribution arrangements to ensure that those arrangements are still valid and up to date. They shall amend product distribution arrangements where appropriate. Insurance distributors that have set up or apply a specific distribution strategy shall, where appropriate, amend that strategy in view of the outcome of the review of the product distribution arrangements. When reviewing their product distribution arrangements, insurance distributors shall verify that the insurance products are distributed to the identified target market. Insurance distributors shall determine the appropriate intervals for the regular review of their product distribution arrangements, thereby taking into account the size, scale and complexity of the different insurance products involved. To support product reviews carried out by manufacturers, insurance distributors shall upon request provide manufacturers with relevant sales information, including, where appropriate, information on the regular reviews of the product distribution arrangements.

[Note: article 10(6) of the IDD POG Regulation]

11 Insurance distributors becoming aware that an insurance product is not in line with the interests, objectives and characteristics of its identified target market or becoming aware of other product-related circumstances that may adversely affect the customer shall promptly
inform the manufacturer and, where appropriate, amend their distribution strategy for that insurance product.

[Note: article 11 of the IDD POG Regulation]

4.3.12 G Manufacturers and distributors should take appropriate action in order to avert the risk of consumer detriment when they consider that the insurance product is not, or is no longer, aligned with the interests, objectives and characteristics of the identified target market.

[Note: recital 12 to the IDD POG Regulation]

4.3.13 EU Relevant actions taken by insurance distributors in relation to their product distribution arrangements shall be duly documented, kept for audit purposes and made available to the competent authorities upon request.

[Note: article 12 of the IDD POG Regulation]

4.3.14 EU Insurance distributors shall set out the product distribution arrangements in a written document and make it available to their relevant staff.

[Note: second sub-paragraph of article 10(1) of the IDD POG Regulation]
In addition to ■ PROD 4.1, ■ PROD 4.2 and ■ PROD 4.3, firms should also consider what needs to be done to comply with obligations found elsewhere in the FCA Handbook, including under the Principles and in SYSC. In considering this firms should consider any relevant guidance.

■ PROD 1.4.10G provides that, where ■ PROD 4 applies, a firm need not apply the guidance in RPPD for matters covered by PROD, if that firm has complied with ■ PROD 4. However, ■ PROD 4 and the IDD POG Regulation does not cover all parts of the RPPD or wider obligations in the FCA Handbook and the following guidance, some of which is reproduced from the RPPD, remains relevant.

Manufacturers should consider whether the design of an insurance product is driven by features that benefit the customer and not by a business model which relies on poor customer outcomes to be profitable.

When providing information to distributors, a manufacturer should:

(1) make it clear if that information is not intended for customer use;

(2) ensure the information is sufficient, appropriate and comprehensible in substance and form, including considering whether it will enable distributors to understand it enough to give suitable advice (where advice is given) and to extract any relevant information and communicate it to the end customer. As part of meeting this standard, the manufacturer may wish to consider, with regard to each distribution channel or type of distributor what information distributors of that type already have, their likely level of knowledge and understanding, their information needs and what form or medium would best meet those needs (which could include discussions, written material or training as appropriate).

When reviewing the insurance products it manufactures, a firm should communicate to the customer and/or distributor contractual “breakpoints” such as the end of a long tie-in period that may have a material impact on a customer that the customer cannot reasonably be expected to recall or know about already.
Manufacturers should act fairly and promptly when handling claims or when paying out on an insurance product that has been surrendered or reached maturity. In doing this, the manufacturer should meet any reasonable customer expectations that it may have created with regard to the outcomes or how the process would be handled.

In ensuring that they have obtained sufficient information about the insurance products they distribute and in ensuring they understand the insurance products distributed, distributors:

1. should consider whether they understand the materials provided by the manufacturer or distributor earlier in the sales chain;

2. should ask the manufacturer to supply additional information or training where this seems necessary to understand the insurance product adequately;

3. should not distribute the insurance product if they do not understand it sufficiently; and

4. when providing information to another distributor in a distribution chain, should consider how the further distributor will use the information, such as whether it will be given to customers. Firms should consider what information the further distributor requires and the likely level of knowledge and understanding of the further distributor and what medium may suit it best for the transmission of information.
Chapter 5

Extended warranties sold with rent-to-own agreements: customer information and deferred opt-in
5.1 Ensuring the customer can make an informed decision

(1) A firm must give the customer the information in (3), at the same time and in the same document, when it offers to sell them an extended warranty.

(2) A firm must ensure that any other person to whom it has referred the customer or invited or induced the customer to obtain an extended warranty from gives the customer the information in (3), at the same time and in the same document, when that person offers to sell the customer an extended warranty.

(3) The information is:

(a) the total cost of the extended warranty, separate from any other prices, in the following terms:

   (i) weekly;

   annually; and

   over the duration of the rent-to-own agreement;

(b) the significant features and benefits, significant and unusual exclusions or limitations of the extended warranty, with cross-references to the relevant warranty document provisions;

(c) a statement that extended warranties may be available from other persons;

(d) an explanation of how the extended warranty interacts with and compares against any other products sold or offered for sale in connection with the rent-to-own agreement (e.g. theft and accidental damage insurance);

(e) an explanation of how the extended warranty interacts with and compares against any standard manufacturer’s warranty that may apply to the goods which are the subject of the rent-to-own agreement, given in a way that enables the customer to make a clear comparison between the two;

(f) when the extended warranty can be concluded, as described in PROD 5.2.1R; and

(g) the date the information in (a) to (f) is provided to the customer.

(4) The information in (3) must be communicated in a way that is:

(a) fair, clear and not misleading;

(b) in writing or another durable medium; and
(c) made available and accessible to the customer.

(5) The information in (3) must be drawn to the customer’s attention and must be clearly identifiable as key information that the customer should read.

5.1.2

(1) A firm that sells extended warranties that constitute contracts of insurance must also comply with the rules in ICOBS 6 (Product Information).

(2) Firms should also take into account the Supply of Extended Warranties on Domestic Electrical Goods Order 2005. Other consumer protection legislation may also be relevant.
5.2 Deferred opt-in for extended warranties

5.2.1  A firm must:

(a) not conclude the sale of an extended warranty; and

(b) ensure that no other person to whom the firm has referred the customer concludes the sale of an extended warranty;

until at least two clear days have passed since the required information was provided to the customer (PROD 5.1.1R).

(2) The period in (1) is one clear day after providing the information if the customer:

(a) initiates the conclusion of the sale of the extended warranty;

(b) consents to the conclusion of the sale of the extended warranty earlier than provided for in (1); and

(c) confirms that they understand the restriction in (1).

5.2.2  For example, if a firm provided the required information to the customer on Monday, it would not (absent the customer’s consent) be able to conclude the sale of the extended warranty until Thursday.

5.2.3  Before the conclusion of the sale of an extended warranty, a firm should have regard to the information needs of its customers and consider whether it would be in the customer’s interest to receive the information in PROD 5.1.1R again, for example if a long time has passed between the provision of the information and the conclusion of the sale.