

# 21

Financial Services Authority

## Implementation of the Distance Marketing Directive

March 2003





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**Annex 1:** Directive 2002/65/EC – Distance Marketing Directive

**Annex 2:** Flowchart: the distance selling and withdrawal process

**Annex 3:** Summary of questions

The Financial Services Authority invites comments on this Discussion Paper. Comments should reach us by 30 April 2003.

Comments may be sent by electronic submission using the form on the FSA's website (at [www.fsa.gov.uk/pubs/discussion/dp21\\_response.html](http://www.fsa.gov.uk/pubs/discussion/dp21_response.html)).

Alternatively, please send comments in writing to:

Jeremy Clivaz  
Business Standards Department  
The Financial Services Authority  
25 The North Colonnade  
Canary Wharf  
London E14 5HS

Telephone: 020 7676 5570

Fax: 020 7676 5571

E-mail: [dp21@fsa.gov.uk](mailto:dp21@fsa.gov.uk)

**It is the FSA's policy to make all responses to formal consultation available for public inspection unless the respondent requests otherwise.**

# 1 Executive summary

- 1.1 The European Council and Parliament adopted the Distance Marketing Directive (DMD) on 23 September 2002. It must be implemented by 9 October 2004.
- 1.2 The DMD aims to protect retail consumers when entering into a financial services contract sold “at a distance”. It applies where there is no face-to-face contact between a supplier and a consumer in the offer, negotiation and conclusion of the contract for the product or service.
- 1.3 The DMD sets out pre-contract information requirements and gives consumers a right to withdraw from a contract.
- 1.4 The FSA will be responsible for implementing the DMD for those firms and activities we already regulate or, in the case of first charge mortgages and general insurance, will regulate in future. The Department of Trade and Industry (DTI) will implement the DMD for consumer credit, second charge mortgages and related activities. We are co-ordinating our implementation work with the DTI and the Treasury, which has overall UK responsibility for implementing the DMD.
- 1.5 Firms conducting designated investment business at a distance are already subject to detailed rules under our Conduct of Business sourcebook. For these firms the structure of our rules will remain largely unchanged, although there will be changes to some of the detail. But for others, notably deposit-takers, we shall be introducing new rules requirements on pre-contract information and withdrawal rights.
- 1.6 This Discussion Paper (DP) looks at the impact of the main provisions of the DMD on different types of firm and seeks information and comments from them, including information on the likely costs of implementation. Responses will help us to prepare draft rules for consultation, which we plan for July 2003.

**Consumers**

This DP will be of interest to consumers because implementation of the directive will, through new rules on pre-contract disclosure and withdrawal rights, give them new or extended protection when buying a financial services product. Consumers will be particularly interested in the new protection they will be given when carrying on business with a bank, building society or credit union at a distance.

# 2 Introduction

## Background

- 2.1 The European Council and Parliament adopted the Distance Marketing Directive (DMD) on 23 September 2002 and it must be implemented by 9 October 2004. A copy of the DMD may be found at Annex 1. It is being implemented by the FSA, the Treasury and the DTI, with the Treasury having overall responsibility for implementation in the UK. Implementation will bring significant changes for some firms, particularly deposit-takers.
- 2.2 The DMD aims to protect consumers when entering into a financial services contract sold 'at a distance'. 'Consumers' are defined as natural persons acting for purposes that are outside their trade, business or profession. The DMD applies where there is no face-to-face contact between a consumer and the firm providing the service, in the offer, negotiation and conclusion of the contract. Examples of the means of communication falling under the DMD are post, internet, fax and telephone.
- 2.3 In order to implement the DMD, we shall be making and amending rules and guidance in our Handbook. Our Conduct of Business sourcebook (COB) imposes detailed conduct of business rules on firms that carry on designated investment business. For these firms, the structure of our rules will remain largely unchanged, although there will be changes to some of the detail. For other firms, notably deposit-takers, we shall have to introduce new rules.
- 2.4 For consumer credit the DTI will introduce the necessary changes to comply with the DMD. We will need to ensure consistent regulation of services subject to both FSA and DTI requirements, for example, banking services.
- 2.5 Where another EEA state has failed to implement the DMD, UK rules can be applied to firms carrying on business from that state with UK consumers.

## **Purpose of this Discussion Paper (DP)**

### **2.6 This Discussion Paper:**

- alerts firms to the impact the DMD will have on their financial services business; and
- seeks comments and information to inform us in the drafting of our rules and preparing a cost-benefit analysis.

### **2.7 The Treasury is planning to issue a consultation document in late Spring 2003. We expect this to set out the Government's approach to the overall UK implementation of the DMD, and the Treasury's views on matters such as the division of responsibility between home and host state authorities.**

### **2.8 We plan to publish a Consultation Paper (CP) with draft rules in late July/early August 2003. In the meantime we would welcome the opportunity to discuss the DMD with firms and their representative bodies, where they would find that helpful.**

## **Which firms and financial services will be affected?**

### **2.9 The DMD applies to "any service of a banking, credit, insurance, personal pension, investment or payment nature". So, it affects substantially all the firms authorised by the FSA that deal with consumers.**

### **2.10 The DMD applies to a single marketing channel: 'distance contracts'. It sets out minimum requirements for information disclosure to consumers about a product or service and requires consumers to be given the right to cancel the contract, although only for a limited range of products.**

### **2.11 In general, the DMD complements rather than replaces earlier directives such as the Third Insurance Directives, UCITS Directive and E-Commerce Directive. For example, the DMD requires the consumer to be given "a description of the main characteristics of the financial service", and, for life insurance products, Annex II to the Third Life Directive contains detailed information requirements that will continue to apply.**

## **Issues of particular relevance to consumers**

### **2.12 The main issues relevant to consumers are:**

- our implementation will, for the first time, apply conduct of business rules to the distance marketing of deposit-based products;



- the DMD aims to protect ‘consumers’ – in effect, private individuals. Some of our current rules for designated investment business also protect small businesses. We ask for views (Chapter 7) whether we should limit our rules to implement the DMD in respect of deposit-taking to ‘consumers’ as defined in the DMD;
- to implement the DMD we shall have to remove the right to cancel for some products when sold by distance means, as explained in Chapter 6. Our provisional view is that we should not remove existing cancellation rights for such products when sold by non-distance means;
- the DMD will not introduce any new complaints or compensation arrangements, but will require disclosure of the arrangements that there are;
- part of the purpose of the DMD is to facilitate cross-border marketing of products and services. It is possible, therefore, that there will be an increase in the range and volume of products and services sold into the UK by firms based in other EEA states. The regulatory arrangements may be different with an increased need for co-operation between the regulatory, complaints and compensation authorities in different jurisdictions.

## **Which parts of our *Handbook* will be affected?**

- 2.13 To implement the DMD we shall have to amend a number of modules in our Handbook, including:

AUTH – Authorisation manual; CIS – Collective Investment Schemes sourcebook; COB – Conduct of Business sourcebook, CRED – Credit Unions sourcebook; ECO – Electronic Commerce Directive sourcebook; ELM – Electronic Money sourcebook; ENF – Enforcement manual;

FREN – Small Friendly Societies sourcebook; PRIN – Principles for Businesses; PROF – Professional Firms sourcebook; SUP – Supervision manual; SYSC – Senior Management Arrangements, Systems and Controls sourcebook; TC – Training and Competence sourcebook.

- 2.14 The DMD requirements will also be reflected in the new sourcebooks we are preparing for our mortgage and general insurance regulation.

## **Disclosure of statutory status and complaints and compensation arrangements**

- 2.15 In CP138 (published in May 2002) we proposed a general framework for firms to disclose their statutory status under the Financial Services and Markets Act 2000 (FSMA) – and to inform customers about complaints and

compensation arrangements. In January 2003 we made rules to require firms to disclose their statutory status in letters, but we deferred decisions on a wider framework. We shall consider this wider framework alongside our implementation of the DMD.

## **Timetable**

- 2.16 Our timetable for consultation and making rules is:
- 30 April 2003 – closing date for responses to this DP;
  - July 2003 – publication of CP with draft rules;
  - 31 October 2003 – end of consultation on CP ;
  - March 2004 – publication of Policy Statement with made rules;
  - 9 October 2004 – rules to come into effect.
- 2.17 We shall be consulting separately on our arrangements for the regulation of mortgages and general (including pure protection) insurance, and our proposals will, so as far as possible, comply with the DMD. Some changes may be made however, in response, to our more general conclusions on implementation of the DMD.

## **Structure of this Discussion Paper**

- 2.18 The rest of this DP is structured as follows:
- Chapter 3 explains the scope of the directive;
  - Chapter 4 explains our options for classifying customers;
  - Chapter 5 explains the pre-contract information requirements set out in Articles 3 to 5 of the directive;
  - Chapter 6 explains the rights of withdrawal required or permitted by Article 6 of the directive and the changes that will be required to our current rules;
  - Chapter 7 summarises the issues for deposit-takers;
  - Chapter 8 discusses cost-benefit issues;
  - Chapter 9 explains next steps.

# 3 The scope of the DMD

## Introduction

- 3.1 The DMD applies to a ‘distance contract’, which is defined (in Article 2 of the DMD – see Annex 1) as:

“any contract concerning financial services concluded between a supplier and a consumer under an organised distance sales or service-provision scheme run by the supplier, who, for the purpose of that contract, makes exclusive use of one or more means of distance communication up to and including the time at which the contract is concluded”.

- 3.2 In this chapter we explore and explain key concepts that arise from this definition: that is, the range of financial services, firms, and, contracts. We consider the consumer definition and connected issues surrounding that in Chapter 4.

## Financial services

- 3.3 The DMD defines ‘financial service’ as “any service of a banking, credit, insurance, personal pension, investment or payment nature”. Therefore, it covers the sale of products such as savings products, insurances and unit trusts, and, agreements for the provision of services such as discretionary management and stockbroking.
- 3.4 The draft revised Investment Services Directive categorises investment advice as a core investment service. On that basis, we consider we should treat ‘investment advice’ as a financial service, and apply our rules implementing the DMD.
- 3.5 We consider that insurance and mortgage intermediation and advice in themselves do not fall within the DMD’s scope. However, an intermediary (as with other intermediaries) will need to comply with the relevant provisions when acting on behalf of a supplier.

## **Firms**

- 3.6 The DMD applies to a financial services ‘supplier’, defined as “any natural or legal person, public or private, who, acting in his commercial or professional capacity, is the contractual provider of services subject to distance contracts”.
- 3.7 So, the directive applies to all the firms authorised and regulated by us when selling financial services to consumers at a distance.
- 3.8 In the UK the purchase of a financial service or product is often arranged through an intermediary (for example, financial adviser, mortgage broker or insurance broker). Where this is the case the DMD allows for a provider’s obligation to provide pre-contract information to be fulfilled by the intermediary, rather than direct by the supplier. In such cases, the DMD will apply only if both the intermediary and the supplier are ‘at a distance’ from the customer.

## **What is a distance contract?**

- 3.9 The DMD applies when the offer, negotiation and conclusion of a contract are carried out purely by “distance means”. That is through direct offer advertising or solely by means such as telephone, post, fax or internet, where there is no “simultaneous physical presence of the supplier and the consumer” (see Recital 15 of the DMD).
- 3.10 Where, however, there is face-to-face involvement by the supplier (or an intermediary acting on the supplier’s behalf) in the offer, negotiation or conclusion of the contract, the DMD does not apply.
- 3.11 Our view is that for a sale to be regarded as a non-distance sale there must be some active involvement between a human agent of the firm and the customer. For example, there will be a distance sale if a customer asks in a branch for a leaflet about a type of product, completes an application off-site and hands it in completed to an employee at the branch. If the customer seeks help in the branch to complete the application or in interpreting the terms it will not be a distance sale.
- 3.12 Recital 18 of the directive explains that “organised distance sales or service-provision scheme” excludes services provided “on a strictly occasional basis and outside a commercial structure dedicated to the conclusion of distance contracts”. Our view is that few firms will be able to take advantage of this exclusion. If a firm provides even the most basic facilities for consumers to deal with it by post or telephone there is sufficient commercial structure for the DMD to apply. Similarly, if an organised scheme exists, even if this is intended to supply other businesses, a one-off sale to a (retail) consumer will fall under the directive.

3.13 E-commerce is one type of distance marketing, and the requirements of the DMD will apply in addition to the specific provisions of the E-Commerce Directive. In implementing the E-Commerce Directive, the UK decided to take advantage of the consumer contracts derogation it allows, but only until the DMD were implemented by other EEA states. We plan to put this into practical effect in our implementation of the DMD.

Q1: Do you agree with our interpretation of the main scope issues?

# 4 Which customers will benefit from the new rules?

## Introduction

- 4.1 There are differences between the DMD definition of ‘consumer’ and the ‘private customer’ classification used for the rules in the Conduct of Business sourcebook (COB) that apply to designated investment business. In this Chapter we explain how we propose to deal with this mismatch and ask for views on our proposals.

## The differences explained

- 4.2 The DMD protections apply to contracts with a ‘consumer’, defined (in Article 2) as “any natural person who, in distance contracts covered by this Directive, is acting for purposes which are outside his trade, business or profession”.
- 4.3 COB requires a firm to give the highest level of protection to a customer classified as a ‘private customer’. For example, the product disclosure rules and cancellation requirements (which are relevant to our implementation of the DMD) apply to firms when dealing with a private customer, but not otherwise.
- 4.4 The two definitions are not the same, for example:
- COB 4.1.9 allows a private individual who is an ‘expert’ to be classified as an intermediate customer, rather than as a private customer; but, such an expert is a ‘consumer’ for the purposes of the DMD;
  - an individual who is acting as trustee is treated as a private customer only if the trust falls within certain size limits; but, every individual acting as trustee is a consumer for the purposes of the DMD;
  - an individual who is an authorised person may not always be treated as a ‘private customer’, even when acting in a private capacity.

- 4.5 The COB private customer classification also goes wider than consumer. For example an individual acting as partner of a smaller partnership (net assets less than £5 million) is classified as a private customer; but, would not be a consumer for DMD purposes.
- 4.6 There is therefore a two way mismatch. Some consumers are not private customers; and, some private customers are not consumers.

## **Our proposals for dealing with the mismatch**

- 4.7 To ensure that all consumers (as defined within the DMD) are provided with the protections that the DMD requires, we propose to retain the existing COB classification system but, for distance contracts, to extend the application of relevant rules across to all consumers (as defined by the DMD) in the areas specifically required by the DMD. An alternative would be to amend the private customer definition so that it caught all consumers. We do not think that such a move would be justified – for example, classification of an expert individual as an intermediate (rather than private) customer can give that expert access to markets and to dealing systems that otherwise would not be available, and, lower costs; similarly, larger trusts will have access to specialist advice and their needs differ considerably from those of private individuals.
- 4.8 We do not, however, propose to cut back the coverage of private customer to match the consumer definition, nor, within our implementation of the DMD, consider other significant change to it.
- 4.9 Where, for distance contracts, the DMD requires or prohibits a specific course of action, our view is it will generally be appropriate to apply rules requiring or prohibiting that action for all private customers – even where they are not consumers. This avoids firms having to adopt a *de facto* additional classification of private customers into individuals and non-individuals, and, the systems costs that would bring.

Q2: Do you agree that we should retain the existing customer classification system for designated investment business, subject to any changes needed to comply with the DMD, as explained in Chapter 4? If not, what do you propose instead?

# 5 Pre-contract information

## Introduction

- 5.1 The DMD sets out detailed requirements for information that must be provided to a consumer. This chapter explains the main requirements and our proposals to implement them.

## The directive's main provisions

- 5.2 Article 3.1 sets out information that must be provided “in good time before the consumer is bound by any distance contract or offer”. This includes information about:
- the supplier, including details of any professional the consumer deals with instead of the supplier;
  - the financial service, including its main characteristics, the total price to be paid, and, notice of “special risks”;
  - the distance contract, including its minimum duration, information on the right of withdrawal (if applicable, see Chapter 6), and, any other early termination rights and penalties;
  - redress, including information about out-of-court complaints and compensation arrangements.
- 5.3 Article 3.3 allows a more limited range of information to be provided to a consumer in the case of telephone sales, subject to “explicit consent”. The consumer must be told the nature of other information available. Full information must be provided on durable medium immediately after conclusion of the contract.
- 5.4 Article 5 specifies that the information set out in Article 3 and the full contractual terms and conditions must be provided to the consumer on paper



or on another “durable medium” in good time before the consumer is bound by the distance contract or offer. Technically, this provision also applies where the initial contact has been made by telephone and the firm has provided only limited information. However, the DMD also provides that where the means of distance communication used does not allow the information to be provided before conclusion of the contract, it must be provided on durable medium immediately after conclusion. This allows a contract to be entered into through a single telephone call.

## **Successive operations**

- 5.5 Article 1.2 provides that where a contract consists of an initial agreement followed by successive operations of the same nature, the DMD provisions apply only to the initial agreement. In our view this means that the pre-contract information need only be provided once in the case of: a regular premium contract, a broking or discretionary management agreement, and a service such as deposit-taking.
- 5.6 Such an agreement must, however, be set up in terms that contemplate “successive operations”, as the DMD also provides that where there is no service agreement and there is a gap of more than one year between operations of the same nature, the information requirements must be complied with.
- 5.7 In our view what is generally referred to as the renewal of a general insurance contract is not a successive operation, albeit the invitation to renew will often be contemplated within the terms of the original agreement (and, will not be prohibited as an unsolicited service by Article 9 of the DMD).

## **Our proposals**

- 5.8 We propose to amend our rules to ensure firms provide the whole of the information that the DMD requires to be provided and that it is provided within the timeframe required by the DMD. We propose to work within our existing framework for information disclosure – for example (where relevant) by adding to the information required to be provided in terms of business. This approach would mean also adding to the information given to customers who are being dealt with face to face (because a common terms of business would be used). We shall only go beyond the strict requirements of the DMD in this way if it is justified on cost-benefit grounds.

5.9 Where our current or proposed rules go beyond the DMD (for example, where they require additional disclosure or a specific format) there is no overriding need to overturn them in favour of the minimum requirements of the DMD. But, we shall be considering whether new cost-benefit issues arise (see Chapter 8).

Q3: Do you agree that we should retain the existing or proposed rules on pre-contract information disclosure as much as possible when implementing the DMD? Are there any instances when this would not be the appropriate way forward?

# 6 Withdrawal rights

## Introduction

- 6.1 Article 6 of the DMD requires consumers to be given the right to withdraw from certain distance contracts once they have been concluded. This chapter explains the main requirements and our proposals to implement them.

## What the DMD requires

- 6.2 Article 6.1 of the DMD provides that a consumer must be given 30 days to withdraw without penalty from a life insurance contract and 14 days from any other contract (we illustrate the process at Annex 2).
- 6.3 However, these withdrawal rights are significantly modified by Article 6.2 which prohibits us from requiring them in respect of financial services whose price depends on fluctuations in the financial market outside the supplier's control. We consider that this will exclude a wide range of financial services that we regulate (when they are sold by distance means) – for example, transferable securities, units in collective investment schemes, and, unit-linked life assurance. This differs from our current rules in COB 6.7, which currently give withdrawal rights for some of these products, but apply 'shortfall' provisions so that the customer and not the supplier bears any cost of a market fall.
- 6.4 The DMD also excludes travel and baggage insurance policies of less than one month's duration from the withdrawal right provisions. For mortgages, we have discretion whether or not to require firms to give withdrawal rights.
- 6.5 In general terms therefore the DMD requires a right of withdrawal for the following when sold by distance means:
- deposit-taking and e-money, for which there is currently no requirement under our rules;

- general insurance (except as noted above) and pure protection insurance, which will be considered through development of our general insurance regime;
- life insurance and personal pensions (other than unit-linked products), which are subject to the existing COB rules; and,
- services such as stock-broking, investment management and investment advice, for which there is currently no requirement.

6.6 The DMD provides that the withdrawal period for distance contracts must begin:

- on the day the contract is concluded, except in the case of life insurance, where it begins on the day the consumer is informed that the contract has been concluded;
- or, if later, the day on which the consumer receives the contractual terms and conditions and pre-contract information.

### **Cancellation of linked contracts**

6.7 Where a financial services contract is linked to another contract, Article 6.7 states that the second contract will also be cancelled without any penalty if the consumer withdraws from the main contract. An example is creditor insurance taken out along with a loan.

### **Payment for services provided before withdrawal**

6.8 Article 7 provides a general principle that where a consumer withdraws from a contract he can be required to pay only for the service actually provided up to withdrawal. This is subject to the following:

- the amount payable by the consumer must be in proportion to the service provided compared to the full coverage of the contract;
- the amount payable cannot be such that it could be viewed as a penalty; and
- the consumer cannot be required to make a payment if the supplier cannot prove the consumer was told the amount payable as part of the pre-contract information; or, the firm commenced performance of the contract without the consumer's prior consent.

### **Fully completed contracts**

6.9 An exemption is provided for contracts “whose performance has been fully completed by both parties at the consumer's express request before the consumer exercises his right of withdrawal”. We interpret this provision as

including insurance contracts where a claim has been made, even though a policy may allow for more than one claim during its term.

## **Our proposed approach**

### **General**

- 6.10 Our proposed general approach is to amend our existing provisions only to the minimum extent necessary to comply with the DMD. This means retaining existing rights of withdrawal for face-to-face business, even where we have to remove them for distance contracts. It also means that where, to implement the DMD, we have to introduce new withdrawal rights (for example, for deposit-taking and e-money) we shall not extend the rights across to face-to-face business.
- 6.11 Where a firm gives withdrawal rights on a voluntary basis, we shall also consider whether controls may be appropriate in order to ensure its customers are treated fairly.

### **Life (including pure protection) insurance and personal pensions**

- 6.12 The Second and Third Life Insurance Directives require a cooling-off period of 14-30 days for most contracts. EEA states have the option of exempting certain contracts, as reflected in COB 6.7. The DMD requires a cooling-off period of 30 days for all life insurance and personal pensions for which it requires withdrawal rights. This means that for distance contacts we shall amend the exemptions set out in COB 6.7.

### **Financial services other than life insurance and personal pensions**

- 6.13 For financial services other than life insurance and personal pensions the withdrawal period laid down in the DMD is 14 days. For distance contracts, we shall align our COB rules with this period.

### **Pre-sale right to withdraw in COB 6.7**

- 6.14 Our rules currently allow a pre-sale right to withdraw from a contract, as an alternative to a right of withdrawal following conclusion of the contract. This right, called a cancellation substitute, is used in particular for pension transfers, because of the difficulty of putting customers back in their original position if a transfer is cancelled. We consider that where the DMD requires a right of withdrawal we cannot retain this pre-sale right.

## **General insurance and mortgages**

- 6.15 What withdrawal rights we require for general (including pure protection) insurance and mortgage products will be decided through our separate consultations on our regulation of these products. However, given the particular circumstances of mortgages our initial view is that we shall not require firms to give a right of withdrawal.

## **Payment for services provided before withdrawal**

- 6.16 Article 7.2 would allow us to introduce rules to require a firm, when a contract is cancelled, to repay the consumer in full. We consider that it will generally be appropriate to operate cancellation arrangements in this way for savings and investment products (that is, where the DMD requires cancellation rights). But, for general insurance, our initial view is that it would be appropriate to allow insurers to charge for cover provided, in order to prevent fraud.

- Q4: Do you agree that we should amend our existing cancellation rules to the minimum necessary to implement the DMD's provisions on rights of withdrawal?
- Q5: Do you agree that for types of business for which there is currently no right of withdrawal for face-to-face business we should not introduce one?
- Q6: Do you have any further comments on our interpretation of and proposals for the withdrawal rights provisions or on the issues arising?

# 7 Implications for deposit-takers

## Introduction

- 7.1 The impact of our implementation of the DMD will be greater on deposit-taking than for many other types of regulated activity. In particular:
- implementation of Articles 3 to 5 (explained in Chapter 5) will bring requirements to disclose significant volumes of information “in good time before the consumer is bound by any distance contract or offer”; and
  - implementation of Article 6 (explained in Chapter 6) will give some customers a rules-based right to withdraw from a contract.
- 7.2 This chapter discusses some of the implications that will be particularly relevant to banks, building societies and credit unions.

## Which firms and operations will be affected?

### General

- 7.3 We consider that the definition of ‘financial service’ within Article 2 of the DMD captures both services and products. For deposits that includes the opening of bank accounts and the sale of deposit-based products – for example, savings accounts, savings bonds and structured deposits (whether or not the customer is an existing account holder).
- 7.4 In broad terms a contract is a distance contract when the offer, negotiation and conclusion of the contract are all carried out without the simultaneous presence of the supplier and the consumer.
- 7.5 So, for deposit taking, our implementation of the DMD will obviously affect call-centre and other telephone operations, internet operations, and paper-based and intermediary marketing operations. However, the boundary between a distance sale and a non-distance sale may be difficult to draw (see

paragraphs 3.9 to 3.12). For example, if literature is on display, it will often be impractical for a firm to ensure that the product is sold only on a face-to-face basis, or, only by distance means.

### **Credit unions**

- 7.6 Our view is that it is only where a firm has no active face to face involvement with a consumer in the offer, negotiation or conclusion of a contract that there can be a distance sale. We believe that there generally is face to face contact with an officer or representative of a credit union, before an individual decides to become a member. Where that is the case, it is likely therefore that there is not a distance sale, so that our rules to implement the DMD will not apply.
- 7.7 Where our rules to implement the DMD do apply, credit union members will benefit from the standardisation of information that the DMD will bring. But, there will also be additional costs for the credit union. We would appreciate information from credit unions about the likely impact of rules to implement the DMD – in particular, to determine the extent to which services are provided ‘at a distance’, about the information that is provided to prospective members and whether implementation of the DMD will require it to be amended, and, about the implications of providing withdrawal rights.

### **Credit and lending operations**

- 7.8 We are not responsible for implementing the DMD for credit and lending operations (beyond our remit to regulate first charge mortgages). Of course, these are often combined with deposit-taking services. We will therefore seek workable solutions to minimise the possibility of conflict between our rules and guidance implementing the DMD for deposit-taking and the requirements for associated lending operations.

### **To which customers should our rules apply?**

- 7.9 The British Bankers’ Association (BBA), Building Societies Association (BSA) and Association for Payment Clearing Services (APACS) sponsor the Banking Code. (There is also a Business Banking Code.) Compliance with the Code is voluntary and is monitored by the Banking Code Standards Board. Not all deposit-takers are signatories to the Code and credit unions are not within its scope.
- 7.10 The Code applies to ‘personal customers’, which includes most but not all individuals acting in a private capacity. The DMD term ‘consumer’ includes all individuals acting in a private capacity. So, the scope of our rules will have to go wider than the Banking Code. We could also seek better alignment with



our proposals for the mortgage regime, or with the definition of ‘private customer’ used in the Conduct of Business sourcebook (but, see Chapter 4 for an examination of the scope differences). The COB definition, for example, includes bodies corporate which are not listed or which have called up share capital or net assets of less than £5m, and, partnerships with net assets of less than £5m.

## **Rights of withdrawal**

- 7.11 The DMD’s provisions and our proposed approach are discussed in Chapter 6. On the approach outlined there, withdrawal rights would be limited to distance contracts and would not also cover face-to-face business.

## **Pre-contract information**

- 7.12 Our Handbook currently imposes only limited COB requirements on deposit-taking (with the exception of cash ISAs). Implementation of the DMD means that we shall have to introduce significant new rules-based requirements for the contracts it covers. In particular, implementation of Articles 3 to 5 will bring requirements to disclose significant volumes of information “in good time before the consumer is bound by any distance contract or offer” about the supplier, the financial service, the distance contract and redress, as explained in Chapter 5.
- 7.13 Although we would need to consider the issues in significant depth before doing so, it would be open to us, subject to consultation, to impose the information requirements of the DMD on all deposit arrangements or a class or classes of them, even if sold face-to-face. Standardising information provision in this way could bring benefits in terms of consumer understanding of any offer, and lead to better consumer decisions.

## **Format and presentation of pre-contract information**

- 7.14 The Code requires a deposit-taker to give a personal customer “clear information explaining the key features of the services and products you tell us you are interested in” and to help the customer understand how the account or service he or she has chosen works.
- 7.15 The DMD does not impose a standard format for the information to be given to consumers. We have found such standardisation to bring benefits for other products, for example, ‘packaged products’ (personal pensions, unit trusts and life policies) and we are proposing a standard format for mortgage illustrations (a Pre-Application Illustration).

7.16 The externally imposed timetable for implementation of the DMD is demanding. We doubt it would be appropriate to seek to specify a presentational format for deposit-based products and services in time for implementation of the DMD. But, doing so would ensure important features of the product and any risks were presented to the consumer in a clear, standard form. This would assist consumers in comparing products and in deciding whether or not the product met their needs. As a minimum, however, we consider we shall have to provide firms with an interpretation of some of the information that the DMD requires. For example, (see DMD Article 3(2)): “a description of the main characteristics of the financial service”, “notice indicating that the financial service is related to instruments involving special risks”.

- Q7: Which deposit-taking operations do you consider will be affected by the DMD? To which deposit-taking contracts should our rules apply? Are there any issues arising which you consider we should take into account in developing our rules and guidance?
- Q8: For credit unions we would like to know in particular the extent to which services are provided ‘at a distance’, about the information that is provided to prospective members and whether implementation of the DMD will require it to be amended, and, about the implications of providing withdrawal rights.
- Q9: Do you consider that in implementing the DMD for deposit-taking we should limit the scope of our requirements to ‘consumers’ as defined in the DMD or apply them to a wider class of customer? If more widely than ‘consumers’, to whom and why?
- Q10: For deposit-taking activities, and in the absence of any regulatory requirement to do so, would firms voluntarily adopt the new DMD-compliant standards for information disclosure for deposit services and products sold other than at a distance? If the answer is yes, for which products and services?
- Q11: For which elements of the Article 3 information requirements do you consider there is particular need for us to provide guidance to deposit-takers?

# 8 Cost-benefit issues

## **Introduction**

- 8.1 Sections 155 and 157 of the Financial Services and Markets Act 2000 (FSMA) require us to carry out a cost-benefit analysis (CBA) of proposed rules and guidance, that is, an analysis of firms' compliance costs, our direct costs and the indirect costs and benefits of our proposals.
- 8.2 In this chapter we explain our preliminary understanding of where the main costs and benefits might arise, and ask respondents for information to inform our CBA.
- 8.3 We will publish a full CBA when we consult on our proposed rules and guidance.

## **Direct costs**

- 8.4 Designing, monitoring and enforcing regulations requires resources. The value of the change in resources absorbed by the regulatory regime in respect of a regulatory change is known as the direct cost of that change. When we consult on our proposed rules for implementing the DMD we shall include a reasonable estimate of the direct costs.

## **Compliance costs - general**

- 8.5 Bringing a product or service to market requires resources not only for production but also for complying with regulation. The value of the extra resources used by firms and individuals to comply with regulatory changes is known as the incremental compliance cost. Resources include time, the costs of changing systems, retraining staff, printing costs and so on. We shall include a reasonable estimate of the incremental compliance costs of our proposals when we consult on our draft rules and guidance. This will be particularly relevant if we make any proposals for rules that go beyond the minimum requirements of

the DMD (that is, super-equivalent proposals) - for example, by applying the DMD requirements to customers or sales channels not within its scope.

## **Compliance costs – impact on different stakeholders**

- 8.6 Our implementation of the DMD will bring different costs to different groups of firms and customers. For firms that operate from branches in the UK we have identified three broad groups.
- 8.7 First, there are firms that carry out activities that are already covered by statutory regulatory requirements similar to those of the DMD. For example, where COB requires them to provide detailed pre-sale information or cancellation rights. For these firms there will be changes to the detail but not to the overall structure of regulatory requirements. For example, there may be changes to the detail of the pre-contract information, to the triggers for and the timing of information provision and to whom precisely information must be provided. These firms have systems to ensure that required information is collated, verified and produced to regulatory requirements, to ensure it is delivered to customers, and that staff know the requirements. However, these firms will incur incremental compliance costs if their systems and procedures need to be modified or replaced. There may also be other costs, such as training or increases in the time it takes to make a sale.
- 8.8 In the second group are firms carrying on activities such as deposit-taking who subscribe to a voluntary code (such as the Banking Code) that requires business practices that are similar to those that will be required upon implementation of the DMD. These firms will have systems similar to those of firms subject to statutory regulation – but, they may not be as rigorous or as defined as will be necessary to comply with our new rules. These firms will incur incremental compliance costs if, as is likely, they have to modify or supplement their systems and procedures. There may also be other costs, such as training or increases in the time it takes to make a sale.
- 8.9 In the third group are firms carrying on activities that for the new regulatory requirements are subject to neither statutory regulation nor to a voluntary code. This includes banks that are not signatories to the Banking Code, e-money issuers and credit unions. For these firms the incremental costs of complying with our rules to implement the DMD may be relatively higher than for firms within the other two groups. They may have to devise and implement new systems, train staff and produce new product literature.
- 8.10 We shall take account of these different stakeholders when carrying out our assessment of firms' compliance costs.

## Indirect costs and benefits

8.11 Regulation also has indirect effects which we shall take into account when considering the costs and benefits of our implementation of the DMD. We generally consider these under four broad categories:

- Quantity of goods sold;
- Quality of goods sold;
- Variety of goods sold; and,
- Efficiency of competition.

8.12 We consider that the DMD may give rise, inter alia, to the following indirect effects:

- where the DMD permits us to go beyond its minimum standards, and were we to do so, it may become relatively more costly for UK-based firms to sell through distance channels within the UK and into other EEA states. This could make the UK a less attractive place to locate;
- if our consumer protection requirements differ from those of other EEA states there could be implications for consumer confusion (where UK and other-EEA regulated firms compete and are subject to different regulation);
- where the DMD allows us little flexibility and we have to remove consumer protection rules, for example in relation to incoming services or withdrawal rights for unit-linked products, consumer protection may be reduced;
- the DMD is not channel neutral and it may therefore distort the relative efficiency of distribution channels. This can affect the efficiency of competition and the strategic decisions of firms.

8.13 There are also benefits from implementation of the DMD.

For consumers:

- there will be the potential for access to a wider range of suppliers and services than before;
- there could be greater competition among suppliers, so prices may fall;
- there will be common minimum standards across a range of products and services supplied at a distance with an increase in consumer understanding and confidence;
- there will be additional cancellation rights for some products in some circumstances which could be valuable.

For firms:

- cross-border entry costs could decrease;

- in the longer-term the common minimum standards introduced through implementation of the DMD could increase consumer confidence in distance sales and mean consumers are more likely to use distance channels.

Q12 Which elements of the DMD's implementation could give rise to significant compliance costs and what types of activity (for example, staff training, printing, transaction times) would give rise to those costs?

Q13 We would like to have respondents' views on the indirect effects of implementation of the DMD: for example, on the use of different distribution channels, and, the impact on the costs and competitiveness of the UK as a location from which to carry on business through distance means with UK persons or into other jurisdictions.

# 9 Next steps

- 9.1 We welcome responses to this Discussion Paper and would appreciate receiving them by 30 April 2003 (but would welcome discussions with firms and their representatives before then). We shall then be considering our policy and preparing a Consultation paper and draft rules and guidance for consultation. We plan to publish this in July or August 2003 and to close consultation on 31 October 2003. After considering responses we shall make the necessary changes to our rules and guidance in about March 2004, to come into force in time for implementation of the DMD on 9 October 2004.





# Directive 2002/65/EC – Distance Marketing Directive

**DIRECTIVE 2002/65/EC OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL**  
**of 23 September 2002**  
**concerning the distance marketing of consumer financial services and amending Council Directive**  
**90/619/EEC and Directives 97/7/EC and 98/27/EC**

THE EUROPEAN PARLIAMENT AND THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community, and in particular Article 47(2), Article 55 and Article 95 thereof,

Having regard to the proposal from the Commission <sup>(1)</sup>,

Having regard to the opinion of the Economic and Social Committee <sup>(2)</sup>,

Acting in accordance with the procedure laid down in Article 251 of the Treaty <sup>(3)</sup>,

Whereas:

- (1) It is important, in the context of achieving the aims of the single market, to adopt measures designed to consolidate progressively this market and those measures must contribute to attaining a high level of consumer protection, in accordance with Articles 95 and 153 of the Treaty.
- (2) Both for consumers and suppliers of financial services, the distance marketing of financial services will constitute one of the main tangible results of the completion of the internal market.
- (3) Within the framework of the internal market, it is in the interest of consumers to have access without discrimination to the widest possible range of financial services available in the Community so that they can choose those that are best suited to their needs. In order to safeguard freedom of choice, which is an essential consumer right, a high degree of consumer protection is required in order to enhance consumer confidence in distance selling.
- (4) It is essential to the smooth operation of the internal market for consumers to be able to negotiate and conclude contracts with a supplier established in other Member States, regardless of whether the supplier is also established in the Member State in which the consumer resides.

(5) Because of their intangible nature, financial services are particularly suited to distance selling and the establishment of a legal framework governing the distance marketing of financial services should increase consumer confidence in the use of new techniques for the distance marketing of financial services, such as electronic commerce.

(6) This Directive should be applied in conformity with the Treaty and with secondary law, including Directive 2000/31/EC <sup>(4)</sup> on electronic commerce, the latter being applicable solely to the transactions which it covers.

(7) This Directive aims to achieve the objectives set forth above without prejudice to Community or national law governing freedom to provide services or, where applicable, host Member State control and/or authorisation or supervision systems in the Member States where this is compatible with Community legislation.

(8) Moreover, this Directive, and in particular its provisions relating to information about any contractual clause on law applicable to the contract and/or on the competent court does not affect the applicability to the distance marketing of consumer financial services of Council Regulation (EC) No 44/2001 of 22 December 2000 on jurisdiction and the recognition and enforcement of judgements in civil and commercial matters <sup>(5)</sup> or of the 1980 Rome Convention on the law applicable to contractual obligations.

(9) The achievement of the objectives of the Financial Services Action Plan requires a higher level of consumer protection in certain areas. This implies a greater convergence, in particular, in non harmonised collective investment funds, rules of conduct applicable to investment services and consumer credits. Pending the achievement of the above convergence, a high level of consumer protection should be maintained.

(10) Directive 97/7/EC of the European Parliament and of the Council of 20 May 1997 on the protection of consumers in respect of distance contracts <sup>(6)</sup>, lays down the main rules applicable to distance contracts for goods or services concluded between a supplier and a consumer. However, that Directive does not cover financial services.

<sup>(1)</sup> OJ C 385, 11.12.1998, p. 10 and OJ C 177 E, 27.6.2000, p. 21.

<sup>(2)</sup> OJ C 169, 16.6.1999, p. 43.

<sup>(3)</sup> Opinion of the European Parliament of 5 May 1999 (OJ C 279, 1.10.1999, p. 207), Council Common Position of 19 December 2001 (OJ C 58 E, 5.3.2002, p. 32) and Decision of the European Parliament of 14 May 2002 (not yet published in the Official Journal), Council Decision of 26 June 2002 (not yet published in the Official Journal).

<sup>(4)</sup> OJ L 178, 17.7.2000, p. 1.

<sup>(5)</sup> OJ L 12, 16.1.2001, p. 1.

<sup>(6)</sup> OJ L 144, 4.6.1997, p. 19.

- (11) In the context of the analysis conducted by the Commission with a view to ascertaining the need for specific measures in the field of financial services, the Commission invited all the interested parties to transmit their comments, notably in connection with the preparation of its Green Paper entitled 'Financial Services — Meeting Consumers' Expectations'. The consultations in this context showed that there is a need to strengthen consumer protection in this area. The Commission therefore decided to present a specific proposal concerning the distance marketing of financial services.
- (12) The adoption by the Member States of conflicting or different consumer protection rules governing the distance marketing of consumer financial services could impede the functioning of the internal market and competition between firms in the market. It is therefore necessary to enact common rules at Community level in this area, consistent with no reduction in overall consumer protection in the Member States.
- (13) A high level of consumer protection should be guaranteed by this Directive, with a view to ensuring the free movement of financial services. Member States should not be able to adopt provisions other than those laid down in this Directive in the fields it harmonises, unless otherwise specifically indicated in it.
- (14) This Directive covers all financial services liable to be provided at a distance. However, certain financial services are governed by specific provisions of Community legislation which continue to apply to those financial services. However, principles governing the distance marketing of such services should be laid down.
- (15) Contracts negotiated at a distance involve the use of means of distance communication which are used as part of a distance sales or service-provision scheme not involving the simultaneous presence of the supplier and the consumer. The constant development of those means of communication requires principles to be defined that are valid even for those means which are not yet in widespread use. Therefore, distance contracts are those the offer, negotiation and conclusion of which are carried out at a distance.
- (16) A single contract involving successive operations or separate operations of the same nature performed over time may be subject to different legal treatment in the different Member States, but it is important that this Directive be applied in the same way in all the Member States. To that end, it is appropriate that this Directive should be considered to apply to the first of a series of successive operations or separate operations of the same nature performed over time which may be considered as forming a whole, irrespective of whether that operation or series of operations is the subject of a single contract or several successive contracts.
- (17) An 'initial service agreement' may be considered to be for example the opening of a bank account, acquiring a credit card, concluding a portfolio management contract, and 'operations' may be considered to be for example the deposit or withdrawal of funds to or from the bank account, payment by credit card, transactions made within the framework of a portfolio management contract. Adding new elements to an initial service agreement, such as a possibility to use an electronic payment instrument together with one's existing bank account, does not constitute an 'operation' but an additional contract to which this Directive applies. The subscription to new units of the same collective investment fund is considered to be one of 'successive operations of the same nature'.
- (18) By covering a service-provision scheme organised by the financial services provider, this Directive aims to exclude from its scope services provided on a strictly occasional basis and outside a commercial structure dedicated to the conclusion of distance contracts.
- (19) The supplier is the person providing services at a distance. This Directive should however also apply when one of the marketing stages involves an intermediary. Having regard to the nature and degree of that involvement, the pertinent provisions of this Directive should apply to such an intermediary, irrespective of his or her legal status.
- (20) Durable mediums include in particular floppy discs, CD-ROMs, DVDs and the hard drive of the consumer's computer on which the electronic mail is stored, but they do not include Internet websites unless they fulfil the criteria contained in the definition of a durable medium.
- (21) The use of means of distance communications should not lead to an unwarranted restriction on the information provided to the client. In the interests of transparency this Directive lays down the requirements needed to ensure that an appropriate level of information is provided to the consumer both before and after conclusion of the contract. The consumer should receive, before conclusion of the contract, the prior information needed so as to properly appraise the financial service offered to him and hence make a well-informed choice. The supplier should specify how long his offer applies as it stands.
- (22) Information items listed in this Directive cover information of a general nature applicable to all kinds of financial services. Other information requirements concerning a given financial service, such as the coverage of an insurance policy, are not solely specified in this Directive. This kind of information should be provided in accordance, where applicable, with relevant Community legislation or national legislation in conformity with Community law.

- (23) With a view to optimum protection of the consumer, it is important that the consumer is adequately informed of the provisions of this Directive and of any codes of conduct existing in this area and that he has a right of withdrawal.
- (24) When the right of withdrawal does not apply because the consumer has expressly requested the performance of a contract, the supplier should inform the consumer of this fact.
- (25) Consumers should be protected against unsolicited services. Consumers should be exempt from any obligation in the case of unsolicited services, the absence of a reply not being construed as signifying consent on their part. However, this rule should be without prejudice to the tacit renewal of contracts validly concluded between the parties whenever the law of the Member States permits such tacit renewal.
- (26) Member States should take appropriate measures to protect effectively consumers who do not wish to be contacted through certain means of communication or at certain times. This Directive should be without prejudice to the particular safeguards available to consumers under Community legislation concerning the protection of personal data and privacy.
- (27) With a view to protecting consumers, there is a need for suitable and effective complaint and redress procedures in the Member States with a view to settling potential disputes between suppliers and consumers, by using, where appropriate, existing procedures.
- (28) Member States should encourage public or private bodies established with a view to settling disputes out of court to cooperate in resolving cross-border disputes. Such cooperation could in particular entail allowing consumers to submit to extra-judicial bodies in the Member State of their residence complaints concerning suppliers established in other Member States. The establishment of FIN-NET offers increased assistance to consumers when using cross-border services.
- (29) This Directive is without prejudice to extension by Member States, in accordance with Community law, of the protection provided by this Directive to non-profit organisations and persons making use of financial services in order to become entrepreneurs.
- (30) This Directive should also cover cases where the national legislation includes the concept of a consumer making a binding contractual statement.
- (31) The provisions in this Directive on the supplier's choice of language should be without prejudice to provisions of national legislation, adopted in conformity with Community law governing the choice of language.
- (32) The Community and the Member States have entered into commitments in the context of the General Agreement on Trade in Services (GATS) concerning the possibility for consumers to purchase banking and investment services abroad. The GATS entitles Member States to adopt measures for prudential reasons, including measures to protect investors, depositors, policy-holders and persons to whom a financial service is owed by the supplier of the financial service. Such measures should not impose restrictions going beyond what is required to ensure the protection of consumers.
- (33) In view of the adoption of this Directive, the scope of Directive 97/7/EC and Directive 98/27/EC of the European Parliament and of the Council of 19 May 1998 on injunctions for the protection of consumers' interests <sup>(1)</sup> and the scope of the cancellation period in Council Directive 90/619/EEC of 8 November 1990 on the coordination of laws, regulations and administrative provisions relating to direct life assurance, laying down provisions to facilitate the effective exercise of freedom to provide services <sup>(2)</sup> should be adapted.
- (34) Since the objectives of this Directive, namely the establishment of common rules on the distance marketing of consumer financial services cannot be sufficiently achieved by the Member States and can therefore be better achieved at Community level, the Community may adopt measures, in accordance with the principles of subsidiarity as set out in Article 5 of the Treaty. In accordance with the principle of proportionality, as set out in that Article, this Directive does not go beyond what is necessary to achieve that objective.

HAVE ADOPTED THIS DIRECTIVE:

#### Article 1

#### Object and scope

1. The object of this Directive is to approximate the laws, regulations and administrative provisions of the Member States concerning the distance marketing of consumer financial services.
2. In the case of contracts for financial services comprising an initial service agreement followed by successive operations or a series of separate operations of the same nature performed over time, the provisions of this Directive shall apply only to the initial agreement.

<sup>(1)</sup> OJ L 166, 11.6.1998, p. 51. Directive as last amended by Directive 2000/31/EC (OJ L 178, 17.7.2001, p. 1).

<sup>(2)</sup> OJ L 330, 29.11.1990, p. 50. Directive as last amended by Directive 92/96/EEC (OJ L 360, 9.12.1992, p. 1).

In case there is no initial service agreement but the successive operations or the separate operations of the same nature performed over time are performed between the same contractual parties, Articles 3 and 4 apply only when the first operation is performed. Where, however, no operation of the same nature is performed for more than one year, the next operation will be deemed to be the first in a new series of operations and, accordingly, Articles 3 and 4 shall apply.

## Article 2

### Definitions

For the purposes of this Directive:

- (a) 'distance contract' means any contract concerning financial services concluded between a supplier and a consumer under an organised distance sales or service-provision scheme run by the supplier, who, for the purpose of that contract, makes exclusive use of one or more means of distance communication up to and including the time at which the contract is concluded;
- (b) 'financial service' means any service of a banking, credit, insurance, personal pension, investment or payment nature;
- (c) 'supplier' means any natural or legal person, public or private, who, acting in his commercial or professional capacity, is the contractual provider of services subject to distance contracts;
- (d) 'consumer' means any natural person who, in distance contracts covered by this Directive, is acting for purposes which are outside his trade, business or profession;
- (e) 'means of distance communication' refers to any means which, without the simultaneous physical presence of the supplier and the consumer, may be used for the distance marketing of a service between those parties;
- (f) 'durable medium' means any instrument which enables the consumer to store information addressed personally to him in a way accessible for future reference for a period of time adequate for the purposes of the information and which allows the unchanged reproduction of the information stored;
- (g) 'operator or supplier of a means of distance communication' means any public or private, natural or legal person whose trade, business or profession involves making one or more means of distance communication available to suppliers.

## Article 3

### Information to the consumer prior to the conclusion of the distance contract

1. In good time before the consumer is bound by any distance contract or offer, he shall be provided with the following information concerning:

#### (1) the supplier

- (a) the identity and the main business of the supplier, the geographical address at which the supplier is established and any other geographical address relevant for the customer's relations with the supplier;
- (b) the identity of the representative of the supplier established in the consumer's Member State of residence and the geographical address relevant for the customer's relations with the representative, if such a representative exists;
- (c) when the consumer's dealings are with any professional other than the supplier, the identity of this professional, the capacity in which he is acting vis-à-vis the consumer, and the geographical address relevant for the customer's relations with this professional;
- (d) where the supplier is registered in a trade or similar public register, the trade register in which the supplier is entered and his registration number or an equivalent means of identification in that register;
- (e) where the supplier's activity is subject to an authorisation scheme, the particulars of the relevant supervisory authority;

#### (2) the financial service

- (a) a description of the main characteristics of the financial service;
- (b) the total price to be paid by the consumer to the supplier for the financial service, including all related fees, charges and expenses, and all taxes paid via the supplier or, when an exact price cannot be indicated, the basis for the calculation of the price enabling the consumer to verify it;
- (c) where relevant notice indicating that the financial service is related to instruments involving special risks related to their specific features or the operations to be executed or whose price depends on fluctuations in the financial markets outside the supplier's control and that historical performances are no indicators for future performances;
- (d) notice of the possibility that other taxes and/or costs may exist that are not paid via the supplier or imposed by him;
- (e) any limitations of the period for which the information provided is valid;
- (f) the arrangements for payment and for performance;
- (g) any specific additional cost for the consumer of using the means of distance communication, if such additional cost is charged;

#### (3) the distance contract

- (a) the existence or absence of a right of withdrawal in accordance with Article 6 and, where the right of withdrawal exists, its duration and the conditions for exercising it, including information on the amount which the consumer may be required to pay on the basis of Article 7(1), as well as the consequences of non-exercise of that right;

- (b) the minimum duration of the distance contract in the case of financial services to be performed permanently or recurrently;
- (c) information on any rights the parties may have to terminate the contract early or unilaterally by virtue of the terms of the distance contract, including any penalties imposed by the contract in such cases;
- (d) practical instructions for exercising the right of withdrawal indicating, *inter alia*, the address to which the notification of a withdrawal should be sent;
- (e) the Member State or States whose laws are taken by the supplier as a basis for the establishment of relations with the consumer prior to the conclusion of the distance contract;
- (f) any contractual clause on law applicable to the distance contract and/or on competent court;
- (g) in which language, or languages, the contractual terms and conditions, and the prior information referred to in this Article are supplied, and furthermore in which language, or languages, the supplier, with the agreement of the consumer, undertakes to communicate during the duration of this distance contract;

#### (4) redress

- (a) whether or not there is an out-of-court complaint and redress mechanism for the consumer that is party to the distance contract and, if so, the methods for having access to it;
- (b) the existence of guarantee funds or other compensation arrangements, not covered by Directive 94/19/EC of the European Parliament and of the Council of 30 May 1994 on deposit guarantee schemes<sup>(1)</sup> and Directive 97/9/EC of the European Parliament and of the Council of 3 March 1997 on investor compensation schemes<sup>(2)</sup>.

2. The information referred to in paragraph 1, the commercial purpose of which must be made clear, shall be provided in a clear and comprehensible manner in any way appropriate to the means of distance communication used, with due regard, in particular, to the principles of good faith in commercial transactions, and the principles governing the protection of those who are unable, pursuant to the legislation of the Member States, to give their consent, such as minors.

#### 3. In the case of voice telephony communications

- (a) the identity of the supplier and the commercial purpose of the call initiated by the supplier shall be made explicitly clear at the beginning of any conversation with the consumer;
- (b) subject to the explicit consent of the consumer only the following information needs to be given:
  - the identity of the person in contact with the consumer and his link with the supplier,
  - a description of the main characteristics of the financial service,

- the total price to be paid by the consumer to the supplier for the financial service including all taxes paid via the supplier or, when an exact price cannot be indicated, the basis for the calculation of the price enabling the consumer to verify it,
- notice of the possibility that other taxes and/or costs may exist that are not paid via the supplier or imposed by him,
- the existence or absence of a right of withdrawal in accordance with Article 6 and, where the right of withdrawal exists, its duration and the conditions for exercising it, including information on the amount which the consumer may be required to pay on the basis of Article 7(1).

The supplier shall inform the consumer that other information is available on request and of what nature this information is. In any case the supplier shall provide the full information when he fulfils his obligations under Article 5.

4. Information on contractual obligations, to be communicated to the consumer during the pre-contractual phase, shall be in conformity with the contractual obligations which would result from the law presumed to be applicable to the distance contract if the latter were concluded.

#### Article 4

##### Additional information requirements

1. Where there are provisions in the Community legislation governing financial services which contain prior information requirements additional to those listed in Article 3(1), these requirements shall continue to apply.
2. Pending further harmonisation, Member States may maintain or introduce more stringent provisions on prior information requirements when the provisions are in conformity with Community law.
3. Member States shall communicate to the Commission national provisions on prior information requirements under paragraphs 1 and 2 of this Article when these requirements are additional to those listed in Article 3(1). The Commission shall take account of the communicated national provisions when drawing up the report referred to in Article 20(2).
4. The Commission shall, with a view to creating a high level of transparency by all appropriate means, ensure that information, on the national provisions communicated to it, is made available to consumers and suppliers.

#### Article 5

##### Communication of the contractual terms and conditions and of the prior information

1. The supplier shall communicate to the consumer all the contractual terms and conditions and the information referred to in Article 3(1) and Article 4 on paper or on another durable medium available and accessible to the consumer in good time before the consumer is bound by any distance contract or offer.

<sup>(1)</sup> OJ L 135, 31.5.1994, p. 5.

<sup>(2)</sup> OJ L 84, 26.3.1997, p. 22.

2. The supplier shall fulfil his obligation under paragraph 1 immediately after the conclusion of the contract, if the contract has been concluded at the consumer's request using a means of distance communication which does not enable providing the contractual terms and conditions and the information in conformity with paragraph 1.

3. At any time during the contractual relationship the consumer is entitled, at his request, to receive the contractual terms and conditions on paper. In addition, the consumer is entitled to change the means of distance communication used, unless this is incompatible with the contract concluded or the nature of the financial service provided.

#### Article 6

#### Right of withdrawal

1. The Member States shall ensure that the consumer shall have a period of 14 calendar days to withdraw from the contract without penalty and without giving any reason. However, this period shall be extended to 30 calendar days in distance contracts relating to life insurance covered by Directive 90/619/EEC and personal pension operations.

The period for withdrawal shall begin:

- either from the day of the conclusion of the distance contract, except in respect of the said life assurance, where the time limit will begin from the time when the consumer is informed that the distance contract has been concluded, or
- from the day on which the consumer receives the contractual terms and conditions and the information in accordance with Article 5(1) or (2), if that is later than the date referred to in the first indent.

Member States, in addition to the right of withdrawal, may provide that the enforceability of contracts relating to investment services is suspended for the same period provided for in this paragraph.

2. The right of withdrawal shall not apply to:

- (a) financial services whose price depends on fluctuations in the financial market outside the suppliers control, which may occur during the withdrawal period, such as services related to:
  - foreign exchange,
  - money market instruments,
  - transferable securities,
  - units in collective investment undertakings,
  - financial-futures contracts, including equivalent cash-settled instruments,

- forward interest-rate agreements (FRAs),
- interest-rate, currency and equity swaps,
- options to acquire or dispose of any instruments referred to in this point including equivalent cash-settled instruments. This category includes in particular options on currency and on interest rates;

- (b) travel and baggage insurance policies or similar short-term insurance policies of less than one month's duration;
- (c) contracts whose performance has been fully completed by both parties at the consumer's express request before the consumer exercises his right of withdrawal.

3. Member States may provide that the right of withdrawal shall not apply to:

- (a) any credit intended primarily for the purpose of acquiring or retaining property rights in land or in an existing or projected building, or for the purpose of renovating or improving a building, or
- (b) any credit secured either by mortgage on immovable property or by a right related to immovable property, or
- (c) declarations by consumers using the services of an official, provided that the official confirms that the consumer is guaranteed the rights under Article 5(1).

This paragraph shall be without prejudice to the right to a reflection time to the benefit of the consumers that are resident in those Member States where it exists, at the time of the adoption of this Directive.

4. Member States making use of the possibility set out in paragraph 3 shall communicate it to the Commission.

5. The Commission shall make available the information communicated by Member States to the European Parliament and the Council and shall ensure that it is also available to consumers and suppliers who request it.

6. If the consumer exercises his right of withdrawal he shall, before the expiry of the relevant deadline, notify this following the practical instructions given to him in accordance with Article 3(1)(3)(d) by means which can be proved in accordance with national law. The deadline shall be deemed to have been observed if the notification, if it is on paper or on another durable medium available and accessible to the recipient, is dispatched before the deadline expires.

7. This Article does not apply to credit agreements cancelled under the conditions of Article 6(4) of Directive 97/7/EC or Article 7 of Directive 94/47/EC of the European Parliament and of the Council of 26 October 1994 on the protection of purchasers in respect of certain aspects of contracts relating to the purchase of the right to use immovable properties on a timeshare basis <sup>(1)</sup>.

<sup>(1)</sup> OJ L 280, 29.10.1994, p. 83.

If to a distance contract of a given financial service another distance contract has been attached concerning services provided by the supplier or by a third party on the basis of an agreement between the third party and the supplier, this additional distance contract shall be cancelled, without any penalty, if the consumer exercises his right of withdrawal as provided for in Article 6(1).

8. The provisions of this Article are without prejudice to the Member States' laws and regulations governing the cancellation or termination or non-enforceability of a distance contract or the right of a consumer to fulfil his contractual obligations before the time fixed in the distance contract. This applies irrespective of the conditions for and the legal effects of the winding-up of the contract.

#### Article 7

##### **Payment of the service provided before withdrawal**

1. When the consumer exercises his right of withdrawal under Article 6(1) he may only be required to pay, without any undue delay, for the service actually provided by the supplier in accordance with the contract. The performance of the contract may only begin after the consumer has given his approval. The amount payable shall not:

- exceed an amount which is in proportion to the extent of the service already provided in comparison with the full coverage of the contract,
- in any case be such that it could be construed as a penalty.

2. Member States may provide that the consumer cannot be required to pay any amount when withdrawing from an insurance contract.

3. The supplier may not require the consumer to pay any amount on the basis of paragraph 1 unless he can prove that the consumer was duly informed about the amount payable, in conformity with Article 3(1)(3)(a). However, in no case may he require such payment if he has commenced the performance of the contract before the expiry of the withdrawal period provided for in Article 6(1) without the consumer's prior request.

4. The supplier shall, without any undue delay and no later than within 30 calendar days, return to the consumer any sums he has received from him in accordance with the distance contract, except for the amount referred to in paragraph 1. This period shall begin from the day on which the supplier receives the notification of withdrawal.

5. The consumer shall return to the supplier any sums and/or property he has received from the supplier without any undue delay and no later than within 30 calendar days. This period shall begin from the day on which the consumer dispatches the notification of withdrawal.

#### Article 8

##### **Payment by card**

Member States shall ensure that appropriate measures exist to allow a consumer:

- to request cancellation of a payment where fraudulent use has been made of his payment card in connection with distance contracts,
- in the event of such fraudulent use, to be re-credited with the sum paid or have them returned.

#### Article 9

##### **Unsolicited services**

Without prejudice to Member States provisions on the tacit renewal of distance contracts, when such rules permit tacit renewal, Member States shall take the necessary measures to:

- prohibit the supply of financial services to a consumer without a prior request on his part, when this supply includes a request for immediate or deferred payment,
- exempt the consumer from any obligation in the event of unsolicited supplies, the absence of a reply not constituting consent.

#### Article 10

##### **Unsolicited communications**

1. The use by a supplier of the following distance communication techniques shall require the consumer's prior consent:

- (a) automated calling systems without human intervention (automatic calling machines);
- (b) fax machines.

2. Member States shall ensure that means of distance communication other than those referred to in paragraph 1, when they allow individual communications:

- (a) shall not be authorised unless the consent of the consumers concerned has been obtained, or
- (b) may only be used if the consumer has not expressed his manifest objection.

3. The measures referred to in paragraphs 1 and 2 shall not entail costs for consumers.

#### Article 11

##### **Sanctions**

Member States shall provide for appropriate sanctions in the event of the supplier's failure to comply with national provisions adopted pursuant to this Directive.

They may provide for this purpose in particular that the consumer may cancel the contract at any time, free of charge and without penalty.

These sanctions must be effective, proportional and dissuasive.



*Article 12***Imperative nature of this Directive's provisions**

1. Consumers may not waive the rights conferred on them by this Directive.
2. Member States shall take the measures needed to ensure that the consumer does not lose the protection granted by this Directive by virtue of the choice of the law of a non-member country as the law applicable to the contract, if this contract has a close link with the territory of one or more Member States.

*Article 13***Judicial and administrative redress**

1. Member States shall ensure that adequate and effective means exist to ensure compliance with this Directive in the interests of consumers.
2. The means referred to in paragraph 1 shall include provisions whereby one or more of the following bodies, as determined by national law, may take action in accordance with national law before the courts or competent administrative bodies to ensure that the national provisions for the implementation of this Directive are applied:
  - (a) public bodies or their representatives;
  - (b) consumer organisations having a legitimate interest in protecting consumers;
  - (c) professional organisations having a legitimate interest in acting.
3. Member States shall take the measures necessary to ensure that operators and suppliers of means of distance communication put an end to practices that have been declared to be contrary to this Directive, on the basis of a judicial decision, an administrative decision or a decision issued by a supervisory authority notified to them, where those operators or suppliers are in a position to do so.

*Article 14***Out-of-court redress**

1. Member States shall promote the setting up or development of adequate and effective out-of-court complaints and redress procedures for the settlement of consumer disputes concerning financial services provided at distance.
2. Member States shall, in particular, encourage the bodies responsible for out-of-court settlement of disputes to cooperate in the resolution of cross-border disputes concerning financial services provided at distance.

*Article 15***Burden of proof**

Without prejudice to Article 7(3), Member States may stipulate that the burden of proof in respect of the supplier's obligations to inform the consumer and the consumer's consent to conclusion of the contract and, where appropriate, its performance, can be placed on the supplier.

Any contractual term or condition providing that the burden of proof of the respect by the supplier of all or part of the obligations incumbent on him pursuant to this Directive should lie with the consumer shall be an unfair term within the meaning of Council Directive 93/13/EEC of 5 April 1993 on unfair terms in consumer contracts <sup>(1)</sup>.

*Article 16***Transitional measures**

Member States may impose national rules which are in conformity with this Directive on suppliers established in a Member State which has not yet transposed this Directive and whose law has no obligations corresponding to those provided for in this Directive.

*Article 17***Directive 90/619/EC**

In Article 15(1) of Directive 90/619/EEC the first subparagraph shall be replaced by the following:

'1. Each Member State shall prescribe that a policyholder who concludes an individual life-assurance contract shall have a period of 30 calendar days, from the time when he was informed that the contract had been concluded, within which to cancel the contract.'

*Article 18***Directive 97/7/EC**

Directive 97/7/EC is hereby amended as follows:

1. the first indent of Article 3(1) shall be replaced by the following:

— relating to any financial service to which Directive 2002/65/EC of the European Parliament and of the Council of 23 September 2002 concerning the distance marketing of consumer financial services and amending Council Directive 90/619/EEC and Directives 97/7/EC and 98/27/EC (\*) applies,

(\*) OJ L 271, 9.10.2002, p. 16.;

2. Annex II shall be deleted.

(1) OJ L 95, 21.4.1993, p. 29.

## Article 19

**Directive 98/27/EC**

The following point shall be added to the Annex of Directive 98/27/EC:

- '11. Directive 2002/65/EC of the European Parliament and of the Council of 23 September 2002 concerning the distance marketing of consumer financial services and amending Council Directive 90/619/EEC and Directives 97/7/EC and 98/27/EC (\*).

(\*) OJ L 271, 9.10.2002, p. 16.'

## Article 20

**Review**

1. Following the implementation of this Directive, the Commission shall examine the functioning of the internal market in financial services in respect of the marketing of those services. It should seek to analyse and detail the difficulties that are, or might be faced by both consumers and suppliers, in particular arising from differences between national provisions regarding information and right of withdrawal.

2. Not later than 9 April 2006 the Commission shall report to the European Parliament and the Council on the problems facing both consumers and suppliers seeking to buy and sell financial services, and shall submit, where appropriate, proposals to amend and/or further harmonise the information and right of withdrawal provisions in Community legislation concerning financial services and/or those covered in Article 3.

## Article 21

**Transposition**

1. Member States shall bring into force the laws, regulations and administrative provisions necessary to comply with this Directive not later than 9 October 2004. They shall forthwith inform the Commission thereof.

When Member States adopt these measures, they shall contain a reference to this Directive or shall be accompanied by such a reference on the occasion of their official publication. The methods of making such reference shall be laid down by Member States.

2. Member States shall communicate to the Commission the text of the main provisions of national law which they adopt in the field governed by this Directive together with a table showing how the provisions of this Directive correspond to the national provisions adopted.

## Article 22

**Entry into force**

This Directive shall enter into force on the day of its publication in the *Official Journal of the European Communities*.

## Article 23

**Addressees**

This Directive is addressed to the Member States.

Done at Brussels, 23 September 2002.

*For the European Parliament*

*The President*

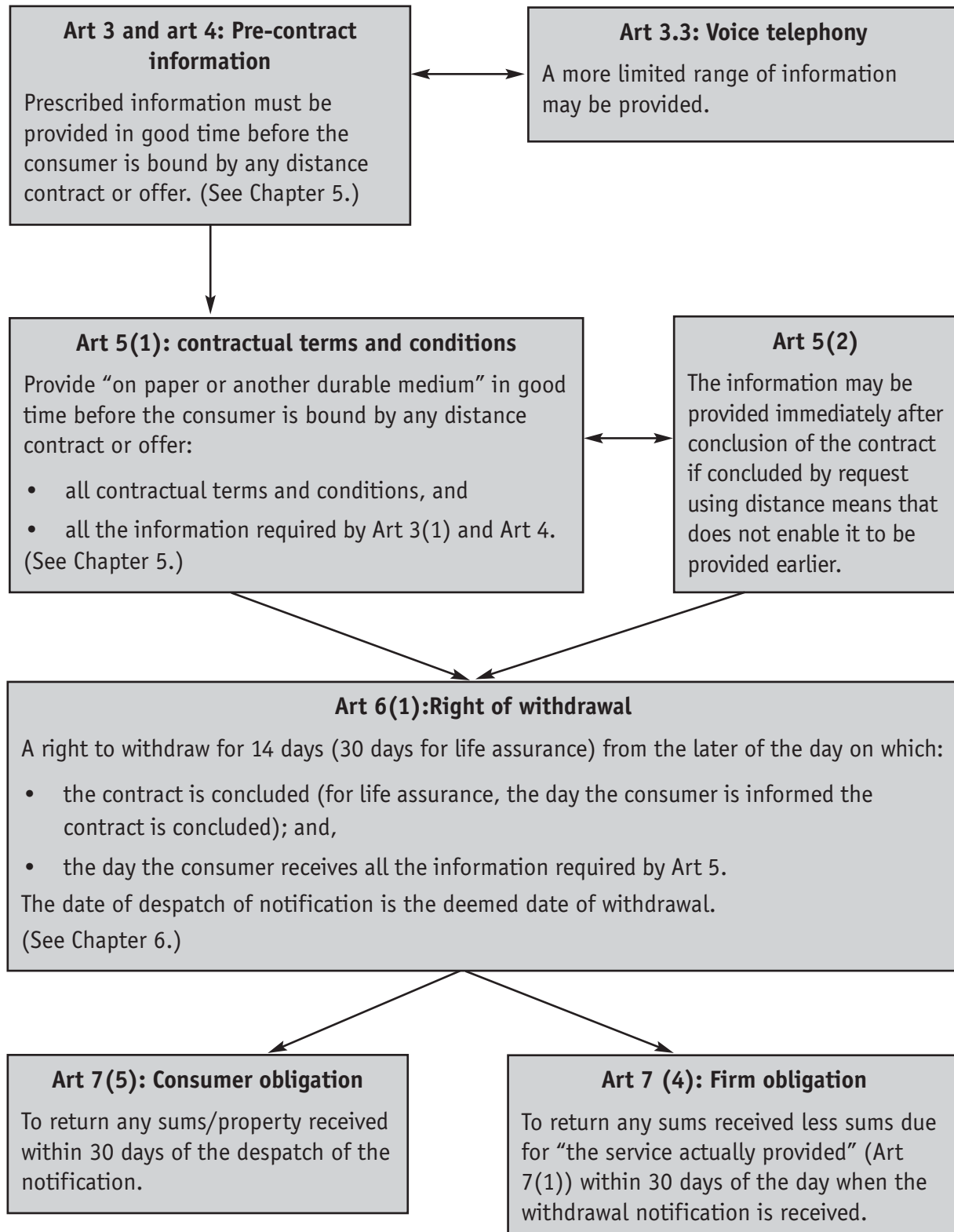
P. COX

*For the Council*

*The President*

M. FISCHER BOEL

# The distance selling and withdrawal process





# Summary of questions

## Chapter 3

- Q1: Do you agree with our interpretation of the main scope issues?

## Chapter 4

- Q2: Do you agree that we should retain the existing customer classification system for designated investment business, subject to any changes needed to comply with the DMD, as explained in Chapter 4? If not, what do you propose instead?

## Chapter 5

- Q3: Do you agree that we should retain the existing or proposed rules on pre-contract information disclosure as much as possible when implementing the DMD? Are there any instances when this would not be the appropriate way forward?

## Chapter 6

- Q4: Do you agree that we should amend our existing cancellation rules to the minimum necessary to implement the DMD's provisions on rights of withdrawal?
- Q5: Do you agree that for types of business for which there is currently no right of withdrawal for face-to-face business we should not introduce one?
- Q6: Do you have any further comments on our interpretation of and proposals for the withdrawal rights provisions or on the issues arising?

## Chapter 7

- Q7: Which deposit-taking operations do you consider will be affected by the DMD? To which deposit-taking contracts should our rules apply? Are there any issues arising which

you consider we should take into account in developing our rules and guidance?

- Q8: For credit unions we would like to know in particular the extent to which services are provided 'at a distance', about the information that is provided to prospective members and whether implementation of the DMD will require it to be amended, and, about the implications of providing withdrawal rights.
- Q9: Do you consider that in implementing the DMD for deposit-taking we should limit the scope of our requirements to 'consumers' as defined in the DMD or apply them to a wider class of customer? If more widely than 'consumers', to whom and why?
- Q10: For deposit-taking activities, and in the absence of any regulatory requirement to do so, would firms voluntarily adopt the new DMD-compliant standards for information disclosure for deposit services and products sold other than at a distance? If the answer is yes, for which products and services?
- Q11: For which elements of the Article 3 information requirements do you consider there is particular need for us to provide guidance to deposit-takers?

## **Chapter 8**

- Q12: Which elements of the DMD's implementation could give rise to significant compliance costs and what types of activity (for example, staff training, printing, transaction times) would give rise to those costs?
- Q13: We would like to have respondents' views on the indirect effects of implementation of the DMD: for example, on the use of different distribution channels, and, the impact on the costs and competitiveness of the UK as a location from which to carry on business through distance means with UK persons or into other jurisdictions.



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The Financial Services Authority  
25 The North Colonnade Canary Wharf London E14 5HS  
Telephone: +44 (0)20 7676 1000 Fax: +44 (0)20 7676 1099  
Website: <http://www.fsa.gov.uk>

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